

In the
Supreme Court of the United States

OCTOBER TERM, 1923

No. 330.

DAYTON-GOOSE CREEK RAILWAY COMPANY }
v. } ss.
INTERSTATE COMMERCE COMMISSION, Etc. }

MOTION FOR LEAVE TO FILE BRIEF
AS AMICUS CURIAE AND TO EXTEND TIME FOR AND
TO PARTICIPATE IN ARGUMENT

And now comes National Association of
Owners of Railroad Securities, by Forney John-
ston, its counsel, and respectfully moves:

1. That leave be granted to movant to file
brief in the above-styled cause as *amicus
curiae*:
2. That the time for oral argument on the
submission of the above-styled cause,
assigned for argument on November
12th, be enlarged by an additional allow-
ance of forty-five minutes, or such time
as the Court may approve, and that
counsel for movant be granted permission
to participate in such oral argument and

be allotted such time as the Court may grant for that purpose by way of extension of the time for argument.

In support of this motion movant respectfully states that the case involves the constitutionality of the so-called excess earnings or recapture provisions of the Transportation Act, 1920 (Section 422, inserting Section 15a in the Interstate Commerce Act) which are deemed by the association of security owners, on behalf of which this motion is made, of general and paramount importance in the process of rate-making for competitive systems of interstate railroad.

The membership of movant includes the owners of a very large proportion of the securities of the American railways—probably in excess of 50 per cent principal amount of the entire funded indebtedness of the Class I railways of the United States—and movant regards the rate-making provisions of the Transportation Act, including the provisions for the adjustment of the competitive rate structure to the economic and constitutional requirements of the several carriers (generally referred to as the excess earnings or recapture clause), as indispensable to the sound and effective regulation of rates for competitive railway systems.

The economic and legal theory of the present rate-making provisions of the Transportation

Act, including the excess earnings clause above mentioned, were presented largely by movant to the Congress during the reconstruction of railway legislation which began with the investigation of the Newlands Committee in December, 1916, and resulted in the adoption of the Transportation Act, 1920; and movant is, accordingly, desirous in the public interest in transportation of presenting to this Court certain legal and economic aspects of the problems which are involved in the question.

Movant has ascertained that the filing of this brief as *amicus curiae* and movant's participation in the argument—should the Court extend the time for oral argument—is agreeable to the Solicitor General and to Counsel for the Interstate Commerce Commission; and has advised counsel for the appellant of its purpose to make this motion without notice of any objection on their part and feels assured that there is no objection.

Respectfully,
JOHN G. MILBURN

FORNEY JOHNSTON,

*Counsel for National Association of
Owners of Railroad Securities.*

November 5, 1923.



IN THE
Supreme Court of the United States

OCTOBER TERM, 1923

No. 330.

DAYTON-GOOSE CREEK RAILWAY CO.,

Appellant,

v.

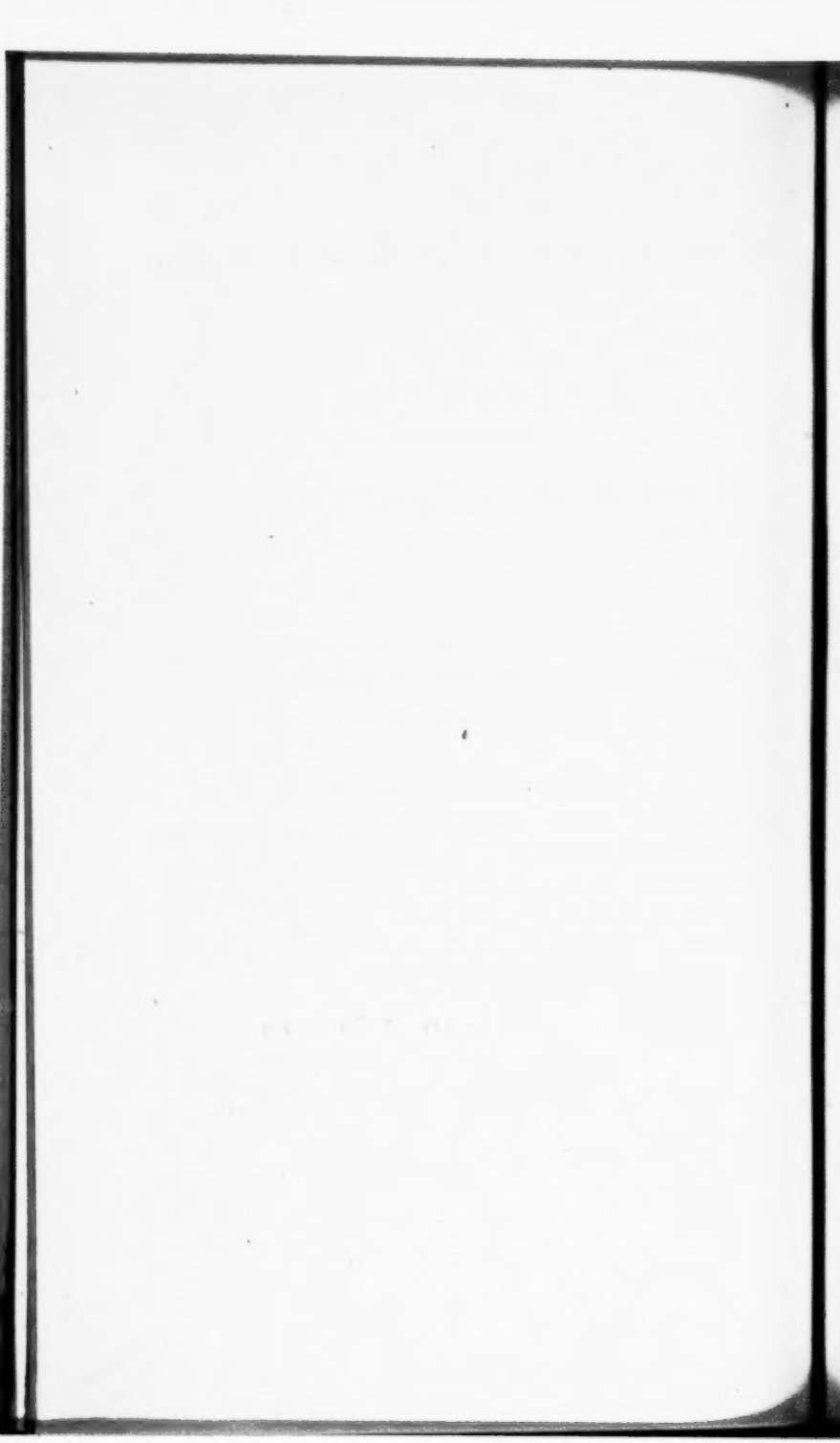
THE UNITED STATES OF AMERICA,
INTERSTATE COMMERCE COMMISSION,
ET ALS., *Appellees.*

BRIEF AND ARGUMENT

On Behalf of Amicus Curiae, National Association of
Owners of Railroad Securities, relative to the consti-
tutionality of Section 15a, Interstate Commerce Act,
as inserted by Section 422 of the Transportation Act
of 1920, Approved February 28, 1920, 41 Stat. L. 488.

John G. Milburn,
FORNEY JOHNSTON,
*Of Counsel for National Association
of Owners of Railroad Securities.*

November, 1923.



INDEX

	Page
Preliminary	3
Due process as contemplated by the statute and by Commission's regulations adequate to correct all minor matters complained of.	5
Excess earnings were admitted by complainant in reports filed by it.	7
Main propositions and authorities.	9
Interest of Amicus Curiae.	22
Legislative dealing with property owners by groups or classes	24
Inter-relation and essential unity of interest between carriers	28
Historic and economic background of Section 15a.	35
Previous inadequacy of the rate-making provisions of the Commerce Act to authorize full considerations of the revenue necessities of the carriers.	40
Controversy and the insoluble problem.	45
Railway credit and revenue the problem before Con- gress	48
Intensive re-survey by Congress of the entire railway problem resulting in Transportation Act, 1920.	51
The group basis for general rate adjustments.	53
The argument against the recapture clause overlooks the fact that it is merely an effective provision for the adjustment of the rate structure to the circum- stances of the individual carriers.	56
Rates adjusted to group requirements.	58
Rates may be tentative or conditional.	59

	Page
Modification of shippers' so-called common law right to destructive competition or to a rate structure that would destroy competitive carriers.....	60
Railroads must survive before they can be forced to compete	62
Adaptation of rate structure to the respective carriers and the principle of classification.....	64
Scope of commerce clause.....	67
Principle not novel.....	68
Fundamental principles plainly sustaining constitu- tionality of Section 15a.....	70
Flexibility in sound regulation.....	75
Further analogies and final observations and sum- mary as to the shipper and the economic justifica- tion for the creation of the excess earning in the first instance.....	77
Intra-State earnings	82
Reserve Fund provisions.....	84
The Principal grounds of opposition to the theory of Section 15(a)	87
New England Divisions Case	92
Appendix	103

TABLE OF CASES CITED

	Page
Akron, Canton & Youngstown Ry. Co. v. U. S. of A. & I. C., June 3, 1922	17
Ames v. Union Pacific, 64 Fed. 165.....	7, 20, 67
A. T. & S. F. Ry. v. U. S., 232 U. S. 199.....	12, 21, 61
A. C. L. R. R. Co. v. Georgia, 234 U. S. 280.....	13
Bauman v. Ross, 167 U. S. 548.....	17, 24
Brunswick & T. Water Dist. v. Maine Water Co., 99 Me. 371, 59 Atl. 537	21, 63
Calder v. Michigan, 218 U. S. 591.....	13
Camden v. Stuart 144 U. S. 104.....	19
C. St. P. & K. C. Ry. Co. Case, 2 I. C. C. 137.....	11, 41, 61
Chicago, Etc., R. Co. v. Iowa, 94 U. S. 155.....	20, 65, 71
Chicago, Etc., R. Co. v. Minnesota, 134 U. S. 418.....	7, 72
Chicago, Etc., R. Co. v. Wellman, 143 U. S. 339.....	20, 67, 72
Commissioner v. Wabash R. Co., 123 Mich. 669, 82 N. W. 526.	20, 67
Cotting v. Stockyards, 183 U. S. 79.....	43
County of Mobile v. Kimball, 102 U. S. 691.....	10
Covington, Etc., Turnpike v. Sanford, 164 U. S. 578.....	17, 65, 70
Daniel Ball, 10 Wall. 557, 564.....	10, 37
Dow v. Beidelman, 125 U. S. 680.....	20, 66
Eastern Advance Rate Case, 20 I. C. C. 243, 261....	11, 16, 50, 61, 64
Fallbrook Irrig. Dist. v. Bradley, 164 U. S. 112.....	15
Fifteen Per Cent Case, 45 I. C. C. 303.....	11, 43, 46
First National Bank v. Union Trust Co., 244 U. S. 416.....	10
Five Per Cent Case, 31 I. C. C. 351; 32 I. C. C. 329..	11, 42, 45, 56, 50
Fletcher, Cyc. Corp. Vol. 8, p. 8635.....	19
French v. Barber Asphalt Co., 181 U. S. 324.....	17, 25
Galveston Electric Co. Case, 258, U. S. 388.....	18

	Page
Georgia, Etc., R. Co. v. Smith, 128 U. S. 174.....	72
Houston, Etc., R. Co. v. Storey, 149 Fed. 499.....	20, 67
Houston, Etc., Ry. v. U. S., 234 U. S. 342.....	10, 37
Houston Telephone Case, 259 U. S. 318.....	18
Houston & T. C. v. Mayes, 201 U. S. 321.....	16, 23
Illinois Light & Traction Co., P. U. R. 1921B, 549.....	18
Increased Rates, 58 I. C. C. 220.....	7
International Harvester Co. v. Kentucky, 234 U. S. 216, 222..	7
I. C. C. v. C. R. I. P. P. Ry. Co., 218 U. S. 88, 109.....	12, 21, 61
I. C. C. v. C. N. O. & T. P., 167 U. S. 479.....	12, 61
I. C. C. v. P. R. R. Co., 222 U. S. 541.....	59
I. C. C. v. Union Pacific R. Co., 222 U. S. 541.....	16, 18, 65, 72, 74
Jackman v. Rosenbaum, Oct. 4, 1922, 260 U. S. 32.....	15, 17
Keogh v. C. & N. W. Ry. Co., 260 U. S. 156.....	11, 22, 40, 61, 79
Kindel Case, 15 I. C. C. 555; 9 I. C. C. 382.....	16, 61
Knoxville v. Water Co., 212 U. S. 1.....	18
Levy Leasing Co. v. Siegel, 258 U. S. 242, 250.....	7, 13
Lincoln Gas Case, 250 U. S. 256.....	18
Louisville, Etc., R. Co. v. Kentucky, 161 U. S. 677, 696.....	35
L. & N. R. Co. v. R. R. Com., 19 Fed. 679.....	21, 69
McCulloch v. Maryland, 4 Wheat 316.....	10
Marcus Brown Holding Co. v. Feldman, 256 U. S. 170.....	13
Mich. Cent. R. R. Co. v. Commission, 236 U. S. 615, 629....	16, 28
Minnesota Rate Cases, 230 U. S. 352.....	10, 18, 20, 69
Missouri v. C. B. & Q. R. R. Co., 241 U. S. 533.....	7
Missouri & Ill. Coal Co. v. I. C. R. R. Co., 22 I. C. C. 39.....	15, 23
Mountain Timber Co. v. Washington, 243 U. S. 219, 243....	17
Munn v. Illinois, 94 U. S. 113.....	71, 84
New England Divisions Case, 66 I. C. C. 197, 261 U. S. 184..	12, 53
Newton v. Consolidated Gas Co., 66 L. ed. adv. op. 305, 308; 258 U. S. 165	18
New York Gas Case, 258 U. S. 165.....	72
New York Passenger Fare Case, 257 U. S. 591.....	52

	Page
New York Cent. R. Co. v. White, 243 U. S. 188, 193.....	21
New York v. United States, et al., 257 U. S. 591.....	12, 83
N. P. Ry. v. Wall, 241 U. S. 87.....	28
Noble State Bank v. Haskell, 219 U. S. 104.....	15, 26
Northern Pac. v. North Dakota, 236 U. S. 585.....	18, 70, 22
Olcott v. Supervisors, 16 Wall 678, 694.....	35
Osborn v. Bank, 9 Wheat 738.....	10
Peck v. Chicago Etc., R. Co., 94 U. S. 164.....	71
Proposed Advances in Freight Rates, 9 I. C. C. 382.....	11, 50
Provident Inst. for Savings v. Malone, 221 U. S. 660....	19, 22, 80
Railroad Comm. of Ala. v. Cent. of Ga. Ry. Co., 170 Fed. (C. C. A.) 225	66
Railroad Comm. v. Illinois, Etc., R. Co., 20 I. C. C. 181, 186..	11, 43
Railroad Comm. of Ky. v. L. & N. R. R. Co. (1904), 10 I. C. C. 173 (187)	15, 27
Ruling Case Law, Vol. 10, p. 15-16, 25 Id. 139-140.....	17
San Joaquin Case, 113 Fed. 930.....	20
St. Louis Land Co. v. Kansas City, 241 U. S. 419, 430....	7, 17, 25
St. L. & S. W. Ry. Co. v. Arkansas, 217 U. S. 136.....	16, 28
Sawyer v. Hoag, 17 Wall 610.....	19
S. A. L. Ry. Co. v. Florida, 203 U. S. 261-9.....	65
Second Employer's Liability Cases, 223 U. S. 1, p. 47.....	10, 37
Sinking Fund Cases, 99 U. S. 700, 719.....	15
Smyth v. Ames, 169 U. S. 466.....	17, 21, 35, 70, 72
Southern Pac. R. Co. v. Darnell, 245 U. S. 531.....	22, 81
Spencer v. Merchant, 125 U. S. 345.....	17, 25
Spokane Case, 15 I. C. C. 376.....	16, 61
Springfield Gas Case, 291 Ill. 209-18; P. U. R. 1920 C, 640-49; 125 N. E. 891.....	18
Stone v. Farmers, Etc., Co., 116 U. S. 307.....	72
Texas v. I. C. C., 258 U. S. 158.....	52
U. S. v. Cohen Gro. Co., 255 U. S. 81.....	7
U. S. v. Joint Traffic Assn., 171 U. S. 505, decided Oct. 24, 1898	11, 41

	Page
U. S. v. Trans-Missouri Freight Assn., 166 U. S. 290.....	11, 41
Wadley Sou. Ry. Co. v. Georgia, 235 U. S. 651.....	7
Wilcox v. Consolidated Gas Co., 212 U. S. 19.....	18, 70
Wilson v. New, 243 U. S. 332.....	21, 78
Wisconsin Passenger Fare Case, 257 U. S. 563.....	12, 21, 52, 83
Wurts v. Hoagland, 114 U. S. 606.....	15, 27

IN THE
Supreme Court of the United States

OCTOBER TERM, 1923

No. 330.

DAYTON-GOOSE CREEK RAILWAY CO.,
Appellant,

v.

THE UNITED STATES OF AMERICA,
INTERSTATE COMMERCE COMMISSION,
ET ALS., *Appellees.*

BRIEF AND ARGUMENT

On Behalf of Amicus Curiae, National Association of Owners of Railroad Securities, Relative to the Constitutionality of Section 15a, Interstate Commerce Act, as Inserted by Section 422 of the Transportation Act of 1920, Approved February 28, 1920, 41 Stat. L. 488.

PRELIMINARY

This brief and argument will deal with the application for preliminary injunction as presenting the single and decisive question of the constitutionality or unconstitutionality on its face, of the provisions of Section 15a of the Transportation Act relating to the regulation or reduction of excess carrier income gratuitously and condi-

tionally allowed the carrier, by requiring one-half of such excess, when ascertained and defined in pursuance of due process, to be paid into a general fund to be administered by the Commission as a by-product of effective rate regulation in the general public interest in transportation, and thus essentially in the interest of the shipping public which has paid the excess.

We conceive that the averments of the bill of complaint are broad enough to indicate a purpose on part of the Commission to press, in due course and in pursuance of the statute, a recovery of one-half of the excess earnings conditionally permitted the Dayton-Goose Creek Railway Company for the last ten months of 1920, and for the year 1921 and for each subsequent year, if and when earned, and that this purpose involves what may be technically termed a threat of a multiplicity of proceedings or suits all involving, if complainant's construction of Section 15a be correct, an identical question of law; viz.: the constitutionality of the theory of that section.

We concede that this situation would give rise to an equity—if we hypothesize the unconstitutionality of the theory of the measure—which might appropriately authorize the issue of an interlocutory injunction pending final hearing. The inconvenience to the Government or the Commission, should a temporary injunction be issued and subsequently dissolved, would be negligible, assuming the solvency of the complainant; and we therefore approach the discussion of the pivotal question, the constitutionality of the excess earnings clause, on the hypothesis that the rules and

regulations already promulgated by the Commission and complied with by the carrier carry the necessary implication of future and continuing action and are therefore orders already promulgated or in process of promulgation within the purview of Sections 208, 211, of the Judicial Code, the Urgent Deficiencies Act of October 22, 1913 (38 Stat. 219), and the Commerce Court Act approved June 18, 1911 (36 Stat. 539), 5 Fed. Stat. Ann. (2d Ed.), p. 1108 *et seq.*

In order that the issue of the constitutionality of the statute on its face—and not erroneous suggestions as to the lack of conformity with due process of the hearings and procedure of the Commission, instant and proposed—may be seen to be the sole and exclusive issue on this submission, it is desirable that we should point out certain misconceptions of the petition.

DUE PROCESS AS CONTEMPLATED BY THE STATUTE AND
BY COMMISSION'S REGULATIONS ADEQUATE TO
CORRECT ALL MINOR MATTERS
COMPLAINED OF

The orders thus far promulgated require the carriers to report the data as to excess earnings to the Commission. They contain a statement of the carrier's duty under the statute in these words, referring to the one-half of the excess reported by the carrier as covered by the excess earnings reduction clause:

*"If unpaid the amount should be paid
by remittance to or draft in favor of the
Interstate Commerce Commission."*

The Director's letter attached to the petition contains a like statement of the carriers' duty

under the Act. These admonitions plainly do not constitute a final or definitive order in the case of any particular carrier or for any specific amount. We entertain no doubt whatever that the statute permits recourse by appellant to the Commission to correct or adjust any of the minor matters complained of by the Dayton-Goose Creek Company. *As to these details* the Commission has made no final or definitive order. *They rest tentatively on appellant's own report.* If, as urged by appellant, the latter itself made a mistake in reporting its valuation on too low a basis, or did not set up appropriate reserves, that may be corrected. There is nothing in the record or in the act or in the regulations to suggest that appellant may not successfully have recourse to the Commission to correct any error or injustice in detail resulting from its own misconception of the procedure or otherwise.

It is to be conceded that the Commission will, perforce, proceed with the administration of the statute after due hearing, or opportunity for hearing, as to the final amount due from this carrier, unless restrained. This brings us to a consideration merely of the constitutional validity of *the basic theory of the Act itself.*

Much of appellant's brief is predicated upon the thought that its own return did not show the actual receipts, expense, income, valuation, or provide for desired adjustments. There is nothing in that situation to sustain injunction. Nothing save unconstitutionality of the provision in its entirety affords the basis for injunction.*

*The statute fully warrants hearing by the Commission before any conclusive adjudication or penal consequences can attach as

EXCESS EARNINGS WERE ADMITTED BY COMPLAINANT
IN REPORTS FILED BY IT

It is to be noted that under the Commission's order of January 16, 1922, and March 16, 1922 (Bill of Complaint, Exhibits "A" and "B"), the aggregate value of the reporting carriers' property called for by the report is the carriers' *own report of value*, adjusted by it to date, made by it in the first general rate adjustment under Section 15a (Ex parte 74, *Increased Rates*, 58 I. C. C. 220); or, if no such return was made, the property investment account of the carrier;† the order specifically providing that "the establishment of preliminary bases for pro-rating the return of six per cent, or ascertaining property values to which the rate is applicable, does not preclude any carrier from using such other bases *as it considers more equitable and in accord with the facts.*"

to any such details. There is nothing in the statute to suggest otherwise. Its plain and necessary implications [Section 15a (9)] are to the contrary. A final order that the carrier shall pay into the fund "all over a reasonable return," with penal consequences attaching to default, might be subject to the consequences of *United States v. Cohen Grocery Company*, 255 U. S. 81; *International Harvester Co. v. Kentucky*, 234 U. S. 216, 222, etc.; but no such consequences can attach to a process of regulation contemplating the recovery, *after hearing*, of one-half of the amount over an ascertained reasonable return tentatively and conditionally permitted. *Levy Leasing Co. v. Siegel*, 258 U. S. 242, 250. The procedure undoubtedly available to the complainant relieves the carrier of the necessity for guessing at the amount involved, with a penalty for guessing wrong. So much for the *statute*, so far as due process is concerned. A like conclusion attaches to the *procedure* before the Commission on that point.

There is nothing in the Act or in the regulations thus far promulgated or threatened suggesting that complainant will be denied a hearing constituting due process within the full significance of the principles announced in *Chicago, etc., R. Co. v. Minnesota*, 134 U. S. 418; *Wadley Southern Ry. Co. v. Georgia*, 235 U. S. 651; *St. Louis Land Co. v. Kansas City*, 241 U. S. 419, 430; *Missouri v. C. B. & Q. R. R. Co.*, 241 U. S. 533; etc.

†A *prima facie* measure fully warranted by the decisions: *Virginia v. West Virginia*, 238 U. S. 202 (*West Virginia Debt Case*); *Ames v. Union Pacific R. R. Co.*, 64 Fed. 165, 177, opinion by Judge Brewer.

This leaves the primary basis of report wholly open to selection by the carrier according to its own notions. On this basis the complainant conceded excess earnings subject to the Act, if valid, *on its own statement of its property value*, for the petition shows on the face of the reports made by the carrier itself (Exhibit C) that the Dayton-Goose Creek Company was permitted a rate level which enabled it to receive under and subject to the conditions of Section 15a and which will permit it to retain permanently the following amounts and ratio:*

Period	Value of property as stated by carrier	Net Railway Operating Income	Division of one-half of excess over 6% payable to general fund under Section 15a as reported by carrier	Approximate annual rate of return received by carrier before applying excess earnings reduction under Section 15a	Approximate annual rate of return received and to be retained by carrier after applying excess earnings reduction under Section 15a
10 months 3-1-20—	\$543,471.97 (Feb. 28, 1920)				
12-31-20....	\$613,994.82 (Dec. 31, 1920)	\$50,746.01 (10 mos.)	\$10,833.12	10.5%	Over 8.2%
Year 1921..	\$699,502.96	\$72,948.95	\$16,883.49	10.4%	Over 8%

For these reasons, on the face of the record and its own return, complainant by its own admission is complaining of a process of regulation which would leave complainant with a return of slightly over 8.2 per cent for the ten months of 1920 and of more than 8 per cent for the year 1921.

It will be well to recall in this connection, and as bearing upon the constructive purpose and intent of Congress in the adoption of Section 15a,

*These figures are based upon the carrier's own reports and not on what the Commission may after notice and hearing find to be the actual rate of return.

the rate of return on their property investment accounts earned by the operating steam carriers of the United States for the period 1908-1921, which is shown below :

Year ended June 30:	Investment	Net railway Operating Income	Return on Investment Per cent
1908.....	\$13,213,766,540	\$634,794,284	4.80
1909.....	13,609,183,515	710,574,052	5.22
1910.....	14,557,816,099	805,097,141	5.53
1911.....	15,612,378,845	744,669,102	4.77
1912.....	16,004,744,966	727,458,036	4.55
1913.....	16,588,603,109	806,800,960	4.86
1914.....	17,153,785,568	674,623,250	3.93
1915.....	17,441,420,382	694,276,111	3.98
1916.....	17,689,425,438	1,002,934,791	5.67
Dec. 31:			
1916.....	17,842,776,668	1,058,505,501	5.93
1917.....	18,574,297,873	952,647,110	5.13
1918.....	18,984,756,478	502,777,017	2.65
1919.....	19,800,120,717	454,969,169	2.36
1920.....	19,849,319,946	15,155,130	.08
1921.....	20,338,597,657	600,986,183	2.95

(36th Annual Report, I. C. C., December 1, 1922, p. 99.)

From these preliminary considerations it is plain that the only question before the court is the broad question of the constitutionality or unconstitutionality *on their face* of the provisions for the regulations or reduction of excess earnings, for the reason that if they can apply to any carrier they admittedly apply to the Goose Creek Company on the facts reported by it; or if those facts were erroneously stated they may be corrected on application to the Commission.

We preface the argument with a summary of the main propositions and authorities asserted.

MAIN PROPOSITIONS AND AUTHORITIES

I

The Commerce Clause of the Constitution confers plenary power on Congress, subject only to the Fifth Amendment, to regulate common car-

riers engaged in interstate commerce by any means having a fair relation to that end and deemed appropriate by Congress.

Minnesota Rate Cases, 230 U. S. 399, 411;

Houston East & West Texas Ry. Co. v. U. S., 234 U. S. 351;

First National Bank v. Union Trust Co., 244 U. S. 416;

McCulloch v. Maryland, 4 Wheat. 316; and

Osborn v. Bank, 9 Wheat. 738.

II

The power to regulate conferred by the Commerce Clause means to "foster," "protect," "conserve"; and our Federal system attaches to every power the necessary implication of duty where the public welfare demands the exertion of the power.

Second Employers' Liability Cases, 223 U. S. 1, 47;

The Daniel Ball, 10 Wall. 557, 577;

County of Mobile v. Kimball, 102 U. S. 691; and

Houston East & West Texas Ry. Co. v. U. S., *supra*.

III

In the process of regulation the United States may impose upon the agencies of interstate transportation a national policy of enforced isolation and competition, such as prevailed to an intensive degree between the date of the adoption of the Sherman Act and the adoption of the more constructive policy of the Transportation Act(a); leaving competing carriers without any lawful right to agree by concerted action on reasonable rate adjustments based on their average requirements and substantially confining the process of rate fixing to a consideration of the reasonableness

of individual rates when proposed or made effective (presumably without concert, although competitive in character) by the individual carriers affected (b).

- (a) *C. St. P. & K. C. Ry. Co. Case*, 2 I. C. C. 137 (Cooley, Chairman, advises cooperation);
U. S. v. Trans-Missouri Freight Assn., 166 U. S. 290 (Mar. 22, 1897);
U. S. v. Joint Traffic Assn., 171 U. S. 505 (Oct. 24, 1898);
Annual Report, Attorney General, for year June 30, 1910, pp. 8 and 9;
28th Annual Report of I. C. C., 1914;
Keogh v. C. & N. W. Ry. Co., 260 U. S. 156;
- (b) *The Five Per Cent Case*, 31 I. C. C. 351, 355, 359;
R. R. Comm. v. Ill., etc., R. Co., 20 I. C. C. 181, 186;
See waivers by carriers necessary to secure consideration in the *Fifteen Per Cent Case of 1917*, 45 I. C. C. 303, 317.

IV

This process and its incidents made remedial rate regulation based on general revenue considerations a problem of exceptional difficulty (note, for instance, the rigid burden of proof—opinion of Commissioner Meyer, in the *Fifteen Per Cent Case*, 45 I. C. C. 303, 331, 334; the fact that certain of the carriers required no higher revenue—the *Five Per Cent Case of 1914*, 31 I. C. C. 351, 384; also the *Fifteen Per Cent Case*, *supra*; and see also the *Advance Rate Cases* reported in 9 I. C. C. 382, 404; and *Eastern Advance Rate Case*, 20 I. C. C. 243, 261) and, accompanied as it was by no effective provision for the control by the Interstate Commerce Commission of the relationship of the intrastate to the interstate rate struc-

ture, based on the important factor of carrier revenue as a primary consideration (*I. C. C. v. C. R. I. & P. Co.*, 218 U. S. 88, 109; *A. T. & S. F. R. Co. v. U. S.*, 232 U. S. 199, and cases cited; *I. C. C. v. C. N. O. & T. P.*, 167 U. S. 479), this condition plainly called for congressional action under the power and duty of conservation inherent in the Commerce Clause. *Message of President Wilson*, Cong. Rec. Dec. 7, 1915 (p. 99); *Newlands (Underwood) Resolution*, Cong. Rec. Feb. 22, 1916, p. 3421; *Wisconsin Passenger Fare Case*, 257 U. S. 563.

V

By the adoption of the Transportation Act Congress reacted to these urgent considerations and evidenced a purpose to deal with the agencies of interstate railway transportation on a basis that would enable them to survive and expand with the necessities of commerce. To that end it conferred on the Commission control over minimum rates, enlarged power over divisions, and announced a new policy as to consolidations, joint use of terminals and facilities, and intercarrier relations. Most important of all, it charged the Commission for the first time with direct and primary responsibility for the initiation and maintenance, on its own motion, of adequate rates for the carriers as a whole or by groups, with power to protect them and to conserve carrier revenue by requiring that the intrastate rate levels be made to conform. *Wisconsin Passenger Fare Case*, 257 U. S. 563; *New York v. U. S.*, 257 U. S. 591; *New England Division Case*, 66 I. C. C. 197; injunction denied in *Akron, Canton & Youngstown Ry. Co. v. U. S.*, June 3, 1922, by Judges Hough, Manton and Mayer, affirmed 261 U. S. 184.

VI

By Section 422 of the Transportation Act (inserting Section 15a in the Interstate Commerce Act) Congress asserted, in pursuance of its plenary power to define the economic necessities revealed to it after the most mature and prolonged inquiry, as a matter of fact binding upon the courts (a fact, moreover, which is within the judicial knowledge of the courts), that it is—

“impossible (without regulation and control in the interest of the commerce of the United States considered as a whole) to establish uniform rates upon competitive traffic which will adequately sustain all the carriers which are engaged in such traffic and which are indispensable to the communities to which they render the service of transportation, without enabling some of such carriers to receive a net railway operating income substantially and unreasonably in excess of a fair return upon the value of their railway property.”

This historic and economic assertion, being an inference obviously justified by the facts ascertained by Congress in the formulation of its post-war policy in regard to railway transportation, can not, legally or rationally, be ignored by the courts. *Levy Leasing Co. v. Siegel*, 258 U. S. 242, 245: “In the enactment of these laws the Legislature of New York did not depend on the knowledge which its members had * * *.” *Marcus Brown Holding Co. v. Feldman*, 256 U. S. 170; *Block v. Hirsh*, 256 U. S. 135.

6 Ruling Case Law, p. 161-2 (Notes 11-13 and cases cited); *Ib.* p. 111, 112, 114, etc., and supplement Vol. 2, p. 31-2; *Muller v. Oregon*, 208 U. S. 412; *A. C. L. R. R. Co. v. Georgia*, 234 U. S. 280; *Calder v. Michigan*, 218 U. S. 591.

VII

Confronted with this ascertained "impossibility"—the long outstanding "insoluble" problem under the old basis of rate fixing—as the only alternative to "regulation and control in the interest of the commerce of the United States" of the excess realized by individual carriers over a reasonable return, built up, as it is, of an excess reflected surely but imperceptibly in each rate, Congress exerted the power of regulation over rates by impressing carrier revenues with a trust, when and as received, for reduction of such excess to the reasonable extent provided by the Act. Section 15a (6) Interstate Commerce Act (Section 422, Transportation Act, 1920).

VIII

By this process Congress proposes to allow the necessary competitive agencies of transportation to survive without contributing gratuitously and unnecessarily to excessive surpluses for individual carriers. The end being lawful and within the express power conferred on Congress to regulate (and conserve) the agencies of interstate transportation and the means adopted having a direct and rational relation to that end, no doubt can exist as to the power of Congress to put the process into effect unless the result is demonstrated to be confiscatory by a carrier complaining on its own account.

Authorities cited, Proposition I.

IX

Nor can doubt exist as to the power of Congress to control and regulate a surplus to accrue in the future, the creation, regulation or application of which is within the competency of Congress. The distinction between legislation dealing with a surplus or revenue received uncondi-

tionally by a carrier *before* the adoption of the legislation and revenue received after the adoption of legislation and subject to the trust thereby established, is fundamental. *Sinking Fund Cases*, 99 U. S. 700, 719; 138 U. S. 84.

X

(a) Congress, or the legislature of a State within its proper sphere, may group owners of property according to a legislatively ascertained community of interest in some public objective, such as an improvement area, a drainage project, or for the purpose of regulation or protection, according to what has been termed an "average reciprocity of advantage, although the advantages may not be equal in the particular case."

(b) No one would suppose that doubt could exist as to the power of Congress to group interstate carriers or to authorize the Commission to divide railroads into competitive groups, or to regard them as components of a single group nation-wide in its scope, for the purposes of more intelligent regulation, in further recognition of the already recognized unity of interstate transportation and of the necessity for emphasizing its essentially national character.

(a) *Wurts v. Hoagland*, 114 U. S. 606;
Fallbrook Irrig. Dist. v. Bradley, 164 U. S. 112;

Noble State Bank v. Haskell, 219 U. S. 104;
Jackman v. Rosenbaum, 260 U. S. 22.

(b) See Interstate Commerce Act as to Carmack Amendment and as to joint routes, etc., and the following authorities as to their joint or inter-carrier relations or interdependence, without statutes and under statutes.

RR. Com. of Ky. v. L. & N. RR. Co. (1904),
10 I. C. C. 173 (187).

Mo. & Ill. Coal Co. v. I. C. RR. Co., 22 I. C.
C. 39;

Mich. Cent. RR. Co. v. Comm., 236 U. S. 615, 629;
Houston & T. C. v. Mayes, 201 U. S. 321;
St. L. & S. W. Ry. Co. v. Arkansas, 217 U. S. 136 (147).

XI

No carrier which engages in interstate commerce has a right superior to the Commerce Clause to force its competitors out of business by competition in rates or, as the only alternative, to demand an excessive return upon the fair value of its property, it being clearly within the competency of Congress to avoid by appropriate regulation both alternatives stated.

I. C. C. v. Union Pacific R. Co., 222 U. S. 541.
Spokane Case, 15 I. C. C. 376.
Eastern Advance Rate Case, 20 I. C. C. 243, 273, 274.
Kindel Case, 15 I. C. C. 555, 9 I. C. C. 382.

XII

A benefit gratuitously conferred by Congress in the course of any lawful public object may be conferred conditionally and subject to an express program for its recovery without violation of the Fifth Amendment. While taxation for benefits conferred is not the process employed in Section 15a, the proposition is of universal application that the recapture of gratuitous benefits conditionally conferred (in this case an excess in rates which the carrier could not demand as of right) under a statute providing for their recovery does not constitute a taking of property; and the fact of benefits, though not the final ascertainment of their amount, may be determined by the legislature. This sound mechanism may be employed under the Commerce Clause.

Jackman v. Rosenbaum, supra, and cases cited Prop. X (a).

10 Ruling Case Law, p. 15-16; 25 id, 139-140.

Bauman v. Ross, 167 U. S. 548.

Spencer v. Merchant, 125 U. S. 345.

French v. Barber Asphalt Co., 181 U. S. 324.

St. Louis etc., Co. v. Kansas City, 241 U. S. 419.

Compare also the Workman's Compensation Cases (*e. g.*, *Mountain Timber Co. v. Washington*, 243 U. S. 219, 243, where the *quid pro quo* is recognized).

XIII

A carrier which has devoted its property to public use is entitled to demand no return in excess of a reasonable return upon the fair value of its carrier property (a). A common process for testing the reasonableness of rates as a whole is to test the result (b). Except in plain cases of confiscation, the courts ordinarily insist upon an actual test before inquiring judicially into their sufficiency (c). There exists no sound reason why Congress may not insist upon the same process for the purpose of regulation that the courts employ for checking the results of regulation. "A just and reasonable rate * * * must often be tentative, since exact results cannot be foretold" (d).

- (a) *Smyth v. Ames*, 169 U. S. 466: "such a corporation was created for public purposes. It performs a function of the State. Its authority . . . was given primarily for the benefit of the public," etc. (p. 544);

Covington, etc., Turnpike v. Sanford, 164 U. S. 578;

Wilcox v. Consolidated Gas Co., 212 U. S. 19;

Minnesota Rate Cases, 230 U. S. 454;

North Pac. R. Co. v. North Dakota, 236 U. S. 585 and cases tabulated;

Galveston Electric Co. Case, 258 U. S. 388.

Houston Telephone Case, 259 U. S. 318.

- (b) *I. C. C. v. U. P. RR. Co.*, 222 U. S. 541:
"Where the rates as a whole are under consideration, there is a possibility of deciding, with more or less certainty, whether the total earnings afford a reasonable return."

Northern Pac. R. Co. v. North Dakota, 236 U. S. 585: "When the question is as to the profitableness of the intrastate business as a whole under a general scheme of rates, the carrier must satisfactorily prove the fair value of the property employed in its intrastate business, and show that it has been denied a fair return on that value."

- (c) *Knoxville v. Water Co.*, 212 U. S. 1;
Willcox v. Consol. Gas Co., 212 U. S. 19;
Lincoln Gas Case, 250 U. S. 256;
Newton v. Consolidated Gas Co., 66 L. ed. adv. op. 305, 308 (one year held sufficient).
- (d) *Springfield Gas Case*, 291 Ill. 209, 218, P. U. R. 1920 C, 640, 649, 125 N. E. 891;
Re Illinois Light & Traction Co., P. U. R. 1921 B, 549.

XIV

A common requirement of the courts in rate cases is to require a complaining carrier to impound a part of higher rates permitted, pending an injunction against the enforcement of lower rates asserted to be confiscatory, and to hold such fund subject to recapture and distribution under direction of the court according as such fund may prove to have been improperly received by the carrier. Is it rational to insist that Congress may

not adopt a less burdensome process than that employed by the courts in order to assure a reasonable return, plus the gratuitous excess allowed by Section 15a, by admonishing the carrier that it may administer the entire proceeds of the rates but must take them subject to the test of actual results and subject to the trusts created by the statute? The objection properly expressed in *Newton v. Consolidated Gas Co.*, *supra*, was that the court should not impound a fund to be disbursed according to a future schedule of rates to be approved by it, as the courts have no rate-making power. Congress and the Commission have that power.

The doctrine of a trust fund, created by statute or in some jurisdictions on general equitable principles, effective only on the judicial ascertainment of certain contingencies, is a familiar tradition in our jurisprudence (a). Is it possible that Congress has less power under the Commerce Clause to get at excess revenue in the most effective way in the public interest in transportation than the courts have in formulating simple processes for the disposition of assets in the interest of those equitably entitled to them? Excess revenue (rates) paid by shippers to certain carriers, under a system of regulation designed to protect their public interest in other carriers by conserving the latter as going concerns, may undoubtedly, under the Commerce Clause, be marshaled in the transportation interest of the public which has paid the excess to be thus regulated (b).

- (a) *Sawyer v. Hoag*, 17 Wall. 610;
Camden v. Stuart, 144 U. S. 104;
Fletcher, Cyc. Corp., Vol. 8, p. 8635.
- (b) *Provident Inst. for Savings v. Malone*,
221 U. S. 660.

XV

The power of the rate-making authority to adapt the rate structure to the circumstances of the different carriers is undoubted. This could be accomplished through a system of classification, such as by classifying carriers according to their earnings(a), length of road(b), or other familiar principle of classification(c).

- (a) *Chicago, etc., R. Co. v. Iowa*, 94 U. S. 155;
Chicago, etc., R. Co. v. Wellman, 143 U. S. 339.
- (b) *Dow v. Beidleman*, 125 U. S. 680.
- (c) *Ames v. Union Pacific*, 64 Fed. 165;
Houston, etc., R. Co. v. Storey, 149 Fed. 499;
Commissioner v. Wabash R. Co., 123 Mich. 669, 82 N. W. 526;
And see Note, 21 Ann. Cas. 191;
14 Roses Notes (U. S. Sup. Ct.) p. 222.

XVI

A classification for taxation based on net income is too familiar to warrant extensive citation, and many statutes incorporating the railroads in early days recognized a limitation upon income (rather than upon rates) as an effective alternative method of regulating the rates themselves. In short, regulation may be made effective at either end of the hopper.

Laws, New York, 1828, Ch. 304, p. 13.

And see early statutes listed in *Minnesota Rate Case*, 230 U. S. 352, at p. 412; also California Act construed in *San Joaquin Case*, 113 Fed. 930, 192 U. S. 201, which allowed rates to be adjusted so as to produce a given per cent upon the investment, and approved a reduction of the return from 18 per cent to approximately

6 per cent (p. 213). Also the statute held void for lack of certainty as to the ratio of return in *L. & N. R. Co. v. Comm.*, 19 Fed. 679.

XVII

A carrier cannot complain of the supposed violation by Congress of the right of a shipper. This familiar maxim is peculiarly applicable in cases of this nature. Compare the attempt of carriers to complain of discriminations against shippers and localities under the Interstate Commerce Act before the question of revenue consideration was brought to the front by the Transportation Act as interpreted in the *Wisconsin Passenger Fare Case*. *I. C. C. v. C. R. I. & P. R. Co.*, 218 U. S. 88, 109; *A. T. & S. F. v. U. S.*, 232 U. S. 199, and cases cited. Note, Ann. Cas. 1915 C, 60.

XVIII

On broader grounds it may be conclusively asserted that a shipper has no vested, common law, or constitutional right as an individual to any kind of rate, reasonable or otherwise. His common law right with reference to businesses affected with a public interest is strictly derivative, as a member of the general public. (See *Smyth v. Ames*, 169 U. S. 466, at p. 544.) By definition it cannot be superior to the interest of the general public affected, in virtue of which alone the so-called right exists at all. Obviously such "right" is subject to modification by Congress, as are all common law rights of the carriers themselves, in the lawful execution of its powers under the Commerce Clause in the public interest in transportation. *Brunswick & T. Water District v. Maine Water Co.*, 99 Me. 371, 59 Atl. 537; *Wilson v. New*, 243 U. S. 332, 347; *N. Y. Cent. R. Co. v. White*, 243 U. S. 188, 198.

XIX

Congress may foreclose the reasonableness and legality of a rate as to a shipper but leave the question open as to the Government. *Keogh v. C. & N. W. Ry. Co.*, 260 U. S. 156.

XX

The legislative authority may provide specifically as to the person (that is, shipper, consignee, or person actually injured) who shall be entitled to recover for an overcharge in a suit for reparation. As the law stands in cases of reparation, the shipper is authorized to recover, although he may have passed the excess to the consignee or on to the general public in the price of the commodity. There is no reason why Congress may not itself administer the amount of any *excess* over reasonable rates reflected in the excess earnings realized under a group rate structure, made up as it is of inadmeasurable items and paid by unascertainable persons, in the transportation interest of the general public which has paid the excess. *Southern Pac. R. Co. v. Darnell*, 254 U. S. 531, 534; *Provident Inst. for Savings v. Malone*, 221 U. S. 660.

INTEREST OF AMICUS CURIAE

Leave having been requested on behalf of National Association of Owners of Railroad Securities to file this brief as amicus curiae, some reference to the interest of that Association in the constitutional question involved is proper.

The Association, through its direct membership, represents a large proportion of the outstanding securities of the American railways. Included in this membership are mutual insurance companies, savings banks, and other mutual insti-

tutions of a public or quasi-public nature owning for permanent investment railway securities amounting in the aggregate to billions of dollars, including alike the securities of roads of high earning power and their less favored competitors. Organized before the entry of the United States into the Great War, this Association and its membership have since that time been actively and continuously interested in the effort to protect the credit and the service of the railroads as a whole. Their interest in the situation is national in its bearing. Their sole objective has been to urge and assist in maintaining a sound attitude on the part of the public and of public authority toward the transportation systems, and, as an indispensable condition to that objective, a just recognition by the carriers themselves of their public obligations and of their relation to transportation as a whole.

In pursuance of this objective the Association advocated the economic necessity for and the constitutional validity of the principles now embodied in Section 15a of the Interstate Commerce Act.

Being definitely convinced that the principle underlying Section 15a is not only sound and valid but that its nullification would break down the last barrier against Government ownership by reviving the "insoluble problem" of rate regulation, the Association was constrained to request leave of this Court to restate the considerations which were undoubtedly regarded by Congress as sufficient not only to warrant but to compel the adoption of Section 15a.

We respectfully submit that a just conception

of the provision can not be attained without a clear recognition of its historic and economic background and of the essential unity and inter-relation of the agencies of interstate transportation.

LEGISLATIVE DEALING WITH PROPERTY OWNERS OF GROUPS OR CLASSES

The grouping of property owners for the purpose of determining their relation to a common objective is well illustrated by the improvement cases, reviewed from their origin in and illustrated by *Bauman v. Ross*, 167 U. S. 548, in which the legislatively ascertained fact that benefit will accrue to the respective individuals of a betterment area, as distinguished from the indirect and general benefits resulting to the public as a whole, is recognized as consistent with due process, provided the particular property owner is accorded a fair hearing before the amount is determined. In short, benefits or gratuities conferred by statute may be recovered under legislative authority, without compensation, provided a fair hearing is given the property owner as to the question of amount. See Propositions X and XII, *supra*.

It is not of present interest to discuss the many classifications of this established legislative process, it being sufficient for our purposes that the gratuitous beneficiaries of any general public objective may be grouped and the amount of the special benefit accruing to each from the process may be recovered by the public. 10 Ruling Case Law, p. 15-16; *Bauman v. Ross*, *supra*.

The fact of the benefit may be conclusively ascertained and declared by the legislature,

Spencer v. Merchant, 125 U. S. 345, *French v. Barber Asphalt Co.*, 181 U. S. 324; 25 R. C. L. p. 139-140; leaving the question of distribution and amount to be determined after some fair hearing. *St. Louis etc. Land Co. v. Kansas City*, 241 U. S. 419; 25 R. C. L. p. 160.

So, under Section 15a, the necessity for grouping and the fact of benefit from grouping through the fixation of rates or acquiescence by Congress in rates at a level necessary to sustain the group, resulting in excessive benefits to individuals of the group, may be determined by the legislature leaving the question of amount to be ascertained after fair hearing.

Another instance of the legislative recognition of group interests *going far and radically beyond the process of Section 15a* is found in the bank guarantee funds under the administration of which, as asserted by the Supreme Court, "there is no denying that by this law (the Oklahoma Depositors' Guaranty Fund) a portion of its property might be taken without return to pay debts of a failing rival in business." In the case of the fund established under Section 15a the fund is intended for employment in floating equipment reserves or otherwise in the general public interest in transportation and not for the gratuitous benefit of a weaker rival. In those cases where loans are made to individual carriers, the objective is public (as in case of farm aid); the loans are made only on adequate security and the transaction is, properly considered, an investment of the revolving fund or its employment in the public

interest in transportation rather than mere aid to an individual carrier.

The theory of Section 15a is, of course, not the same as in the bank guaranty case, but what was said in *Noble State Bank v. Haskell*, 219 U. S. 104, as to the police power under consideration in that case, is plainly applicable to the *power of regulation* under the Commerce Clause. The latter is not a police power merely. It is a power to conserve the whole as well as to regulate the parts or agencies; so it includes all analagous exertions of the police power, among which is the power to give due consideration to the community of interest and inter-dependence which exists between the agencies engaging in businesses subject to public regulation. As said by the court in the *Haskell Case*, *supra*, with reference to banks, and as is plainly pertinent to the case of interstate railroads whose earnings and functions are directly subject to regulation in the public interest in transportation, "the power to compel beforehand, co-operation, and thus, it is believed, to make a failure unlikely and a general panic almost impossible, must be recognized, if the Government is to do its proper work, unless we can say that the means have no reasonable relation to the end." No interstate railroad can survive and flourish, certainly not as an agency of interstate commerce, unless its connections are enabled to survive on a wholesome basis, and this can be accomplished only by adjustment of the rate structures to their respective reasonable necessities.

The power of the State, and, *a fortiori*, the power of Congress under the Commerce Clause, to

deal with the owners of property in their common or group relationship, could not be better illustrated than by the observations quoted by the Court in *Wurts v. Hoagland*, 114 U. S. 606, with reference to the enjoyment of strictly private property—in that case lands having a general or common relationship to the necessity for drainage:

"It is the power of the government to prescribe public regulations for the better and more economical management of property of persons whose property adjoins, or which, from some other reason, can be better managed and improved by some joint operation, such as the power of regulating the building of party walls; making and maintaining partition fences and ditches; constructing ditches and sewers for the draining of uplands or marshes, which can more advantageously be drained by a common sewer or ditch. This is a well-known legislative power, recognized and treated of by all jurisconsults and writers upon law through the civilized world; a branch of legislative power exercised by this State before and since the adoption of the present Constitution, and repeatedly recognized by our courts. The legislature has power to regulate these subjects, either by general law or by particular laws for certain localities or particular and defined tracts of land. When the Constitution vested the legislative power in the Senate and General Assembly, it conferred the power to make these public regulations as a well-understood part of that legislative power."

The inter-dependence of interstate carriers is well illustrated in relation to one of the fundamentals of transportation, such as car interchange, by the decisions and discussions in *R. R. Com. of Ky. v. L. & N. R. R. Co.* (1904), 10 I. C. C. 173 (187), and the group of cases cited in that opinion, which preceded the adoption of the provisions

of the Commerce Act relating to interchange of loaded cars, through routes, etc. After the latter provisions became effective, the following decisions out of a multitude are typical of the resulting relation: *Missouri & Ill. Coal Co. v. I. C. R. R. Co.*, 22 I. C. C. 39, and *Mich. Cent. R. R. Co. v. Commission*, 236 U. S. 615, 629.

And see *Houston & T. C. v. Mayes*, 201 U. S. 321; *St. L. & S. W. Ry. Co. v. Arkansas*, 217 U. S. 136 (147), as to interchange car relations, and the line of decisions construing the Carmack Amendment, such as *N. P. Ry. v. Wall*, 241 U. S. 87, etc.

We cite later the decisions relating to the rational extension of the integral or group theory of rate regulation made effective by the Transportation Act. The above references are merely to preface the fact that there is a relation between interstate carriers in respect to the problem of rate regulation as inevitable as that involving their physical functions of car supply, interchange, etc., and that a group basis for rate making is within the rational discretion of Congress.

INTER-RELATION AND ESSENTIAL UNITY OF INTEREST BETWEEN CARRIERS

Individual interstate carriers can no more hope to survive and flourish on the wreckage of their interchanges than an individual can hope to flourish in a panic or a nation in a world in chaos. It is not to be supposed that the Commerce Clause and the Fifth Amendment, or the courts in their interpretation of either, are blind to practical considerations which are known to everyone else. These considerations form so definite and so in-

separable a part of the theory, objective and result of Section 15a that the indulgence of the Court is urged for their careful statement in this brief, for no question more important to the survival of the existing system of transportation or to the fate of over twenty billions of dollars of investments in American railways can be brought indirectly before the Courts than is presented by the attack, made in this proceeding by the Dayton-Goose Creek Railway Company, and sundry associated railroads, upon the underlying basis of the rate-making provisions of the Transportation Act.

The chief objections urged before Congress to the validity of this legislation were assertions that it violated the due process and compensation clauses of the Fifth Amendment *as to the carriers* subjected to the regulation and that it interfered with some supposed constitutional right of *shippers*. To these objections have been added in the present case the suggestion of the bill of complaint that the regulation in some way invades the legitimate province of the State in respect to intra-state rates. The former were stated in a letter from former Justice Charles E. Hughes to the Association of Railway Executives, which opposed the legislation before Congress and retained Mr. Hughes to state the case for the opposition. The letter is dated September 19, 1919, and was filed with the committees of Congress during their hearings in the course of the formulation of the Transportation Act, 1920.* We may assume that

* Hearings, House Committee, Return of Railroads to Private Ownership, p. 2981.

it states as cogently as possible the case for the opposition to Section 15a in its preliminary form.

Mr. Hughes' opinion was directed to the original or tentative draft of Section 6 of the Senate Bill which was materially different from the provisions of Section 15a as finally adopted. The main provision of Section 6 relating to the regulation of excess earnings, familiarly called the recapture clause, on which Mr. Hughes' opinion was invited and given is set out in the margin, as set out in his letter.*

As will be noted, the condensed statement of the principle of regulation through recapture thus set out in the original Senate draft omitted provisions essential to a thorough exposition of the theory now found in Section 15a, viz: the provisions stating the economic basis and necessity for the measure now embodied in sub-paragraph (5) of Section 15 (a), which deliberately recognizes and provides that excessive rates may be tentatively and conditionally allowed to be charged by partic-

* If any carrier shall receive from operation in any year more than a fair return, to be determined by the commission, upon the value of its property, held or used for service in transportation, which may include a just allowance to provide reasonably for future years in which there may be insufficient earnings, the excess above such fair return shall be paid to the board within the first four months of the succeeding year, to be invested or expended for the following purposes, namely: One-half of all such payments to the board shall be invested or expended for the purposes set forth in Section 25 hereof, and one-half thereof shall be deposited in a fund which, from time to time, shall be expended by the board in the purchase of equipment to be leased under proper terms to carriers in order to facilitate transportation, or to loan to carriers upon reasonable security in order to purchase equipment or other facilities in the event that such carriers are unable to secure elsewhere the funds with which to provide themselves with adequate transportation facilities. In no event shall surplus earnings in excess of the amount sufficient to pay a fair dividend, whether represented in reserves or otherwise invested in the property of the carrier, be capitalized or used in any way as a basis for increased rates." (From Section 6 of the Senate bill.)

ular carriers on a level high enough to enable their competitors to survive as a gratuitous and recoverable benefit, and that all revenues from such excessive rates are to be regarded as conditional and as received in trust, subject to regulation through subsequent recapture and administration in the interest of transportation as a whole. Section 15(a) (5) stating plainly this condition reads as follows:

"(5) Inasmuch as it is impossible (without regulation and control in the interest of the commerce of the United States considered as a whole) to establish uniform rates upon competitive traffic which will adequately sustain all the carriers which are engaged in such traffic and which are indispensable to the communities to which they render the service of transportation, without enabling some of such carriers to receive a net railway operating income substantially and unreasonably in excess of a fair return upon the value of their railway property held for and used in the service of transportation, it is hereby declared that any carrier which receives such an income so in excess of a fair return, shall hold such part of the excess, as hereinafter prescribed, as trustee for, and shall pay it to, the United States."

The Senate draft criticized by Mr. Hughes also lacked the administrative provision, so desirable to assure due process, that the Interstate Commerce Commission shall prescribe reasonable rules and regulations for the determination and recovery of the moiety of the excess over a reasonable

return, which is now found in sub-section (9). The importance of this provision from a constitutional standpoint lies in the fact that it contemplates a full and orderly hearing and opportunity to the carrier in each case within the purview of the principles of due process referred to above.

Mr. Hughes' opinion upon the legislation in its final form was either not invited or not made public. The Conference Committee which finally agreed on the present draft of Section 15a included upon its membership such distinguished lawyers as Senators A. B. Cummins of Iowa, Atlee Pomerene of Ohio, Frank B. Kellogg of Minnesota, former president of the American Bar Association, Miles Poindexter of Washington, and Joseph T. Robinson of Arkansas, together with the Honorable John J. Esch, then Chairman of the House Committee on Interstate and Foreign Commerce, and now a member of the Interstate Commerce Commission. That committee in particular and the Congress as a whole had before it the views of the distinguished jurist and were not constrained to accept the theory of unconstitutionality thus urged.

In reply to this opinion of Mr. Hughes, a memorandum sustaining the validity of this provision was filed by the Advisory Counsel of the Association of security owners, Messrs. Elihu Root, John G. Milburn, John S. Miller, Hugh L. Bond, and Forney Johnston (House Hearings, *ubi sup.*, pp. 3001, 3009), in connection with which the following observation in the oral presentation of the matter to the Committee may be pertinent:

"It is important to bear in mind that the process of excess earnings regulating is based upon the establishment of rates upon a group basis—rates necessary to sustain transportation in each group. No shipper has a right to complain of rates necessary to sustain transportation considered in the aggregate. No carrier who is given rates higher than it would receive if the rates were considered solely on an individual rate or individual carrier basis can complain if Congress impresses a trust upon the excess.

"It could authorize this excess to be returned to the shippers, but that would be impracticable as the excess involved in each shipment would be negligible.*

"So Congress can clearly deal with this excess which is a by-product of the rational exertion of the commerce power in the general public interest in transportation."

Observations by Mr. Taft, in a special analysis of the Senate Bill forming one of a series of public papers in the Public Ledger during the consideration of the legislation, is of such intrinsic soundness, wholly without reference to his subsequent elevation to the position of Chief Justice, that they are set out in an appendix; as are the remarks by the then Director General (Mr. Hines), and by the late Judge Prouty.

In support of the principle and necessity of this legislation the executives of by far the largest

*And would, moreover, as we will point out, either defeat the object by destroying the competitive uniformity of the rates or result in potential discrimination as between shippers. *Keogh v. C. & N. W.*, *infra*.

single owners for permanent investment of American railroad securities urged the retention of the principle formulated in the Senate draft, asserting that:

"The only thing 'confiscated' is the opportunity for what may fairly be termed excessive return on the value of the investment."*

This expression was followed by a communication to the conferees on December 26, 1919, from like sources representing in that single communication an investment in American railroad securities in excess of two billion dollars; and the legislation as a whole had been urged upon the committees of the House and Senate by a memorial signed by more than 30,000 of the investing institutions and investors of the United States, directly representing an ownership of over \$9,000,000,000 of outstanding railroad securities and approximately 80 per cent of the resources of the United States ordinarily available for investment in railroad securities.

It goes without saying that this impressive group of owners of railroad securities could not have urged upon Congress the adoption of a proposal so novel, when superficially regarded, as the clause for encouragement of adequate rate levels,

*From "A Statement to the Public," Congressional Record, December 18, 1919, by Darwin P. Kingsley (president New York Life Insurance Company); Haley Fiske (president Metropolitan Life Insurance Company, New York); John J. Pulleyn (president Emigrant Industrial Savings Bank, New York); W. D. Van Dyke (president Northwestern Mutual Life Insurance Company, Milwaukee, Wis.); Louis F. Butler (president The Travelers' Insurance Company, Hartford, Conn.); and George F. Johnson (president Penn Mutual Life Insurance Company, Philadelphia, Pa.), Subcommittee.

by the regulation of excess earnings without the most profound conviction as to its economic necessity. The basis for this conviction and at the same time the impregnable constitutional basis for the legislation may well be introduced by a brief survey of the transportation problem as it existed during the period culminating with the seizure of the railroads by the President under the proclamation of December 26, 1917. It will be plain that the chief difficulty—the so-called insoluble problem—had been the difficulty of adjusting a competitive rate structure to the circumstances of the different carriers, the key log of the jam which was solved by Section 15a and is now assailed by the Dayton-Goose Creek Company.

HISTORIC AND ECONOMIC BACKGROUND OF SECTION 15A

Continental transportation may properly be stated to fall within the functions and affirmative obligations of government. *Olcott v. Supervisors*, 16 Wall, 678, 694; *Louisville, etc., R. Co. v. Kentucky*, 161 U. S. 677, 696; *Smyth v. Ames*, 169 U. S. 466.

The maintenance of highways has been governmental in character from time immemorial. The combination of the commerce, post roads and military clauses of the American Constitution bring transportation peculiarly within the group of duties imposed upon the general government. The opposition to Government ownership in America must rest, therefore, not upon constitutional theory, but upon the fact that if the railroads were taken over by the United States they would cease to be a competitive or regulated public

service and would so radically increase the waste, complexity and class reactions of the Federal organism as to constitute a menace to our social and economic institutions.

No one doubts the repugnance of the idea of Government ownership of railroads to established American political and economic theory—not because of the thought that the agencies of transportation may not constitute a function of Government in the sense above stated, but because of a deep and national conviction that Government ownership and/or operations would be justified only in case of the most exigent national and economic needs of our people; yet no one supposes that transportation will be allowed to break down or the people of any substantial geographical area to starve or to freeze, or to sustain grossly unequal burdens from car shortage or other inadequacy of transportation, without intervention by the general Government by virtue of its reserved powers under the commerce, post roads and war powers of the Constitution.

In so far as the agencies of interstate transportation are concerned it is indisputable that the power to regulate conferred by the Commerce Clause is not a mere negative or restrictive power. Inherent in the power are affirmative and constructive elements. Power reserved in the public interest carries a necessary implication of the duty to assert it when necessary. The following quotations are sufficient to make it plain that the Commerce Clause is not a mere negative or repressive provision:

"To 'regulate' in the sense intended is to foster, protect, control, and restrain, with appropriate regard for the welfare of those who are immediately concerned and the public at large." (*Second Employer's Liability Cases*, 223 U. S. 1, p. 47.)

"Congress is empowered to regulate; that is, to provide the law for the Government of interstate commerce; to enact 'all appropriate legislation for its protection and advancement' (the *Daniel Ball*, 10 Wall. 557, 564); to adopt measures to 'promote its growth and insure its safety' (*County of Mobile v. Kimball*, 102 U. S. 691); 'to foster, protect, control and restrain.'" (*Second Employer's Liability Cases*, *supra*; *Houston, etc., Ry. v. U. S.*, 234 U. S. 342, 351.)

The grave and recurrent crises affecting the American railroads and threatening the duration of private ownership and operations under then existing methods of regulation were well known to Congress at the time of the formulation and adoption of the Transportation Act. Whether right or wrong as to the accuracy of the conviction, the Administration had taken over the railroads as a whole because of the impression that they were not sufficiently co-ordinated under private ownership and management as restricted by existing laws to meet the exigencies of transportation confronting the nation on December 26, 1917. While the measure was in conference the Director General (Secretary of the Treasury McAdoo), with the approval of the President, was

urging upon the Committees of both Houses a four or five-year extension of Federal operation of railroads.*

It is not to be denied that Congress recognized and reacted to the most definite understanding of the doubt whether, under the conditions arising out of the war and Federal control and under the disturbed economic relation of wages and costs and the prices of farm and other commodities to the cost of transportation, private ownership and operation could survive. Certainly they could not be expected to endure without the most courageous and constructive treatment of the entire problem, in process of which the full power and duty of conservation inherent in the Commerce Clause clearly had to be invoked to avoid the more drastic alternative of continued Federal operation or ownership. The full significance of the obligation of the Government to the railroads arising out of their seizure by the President is not always recognized. These conditions sensibly increased the necessity for relieving the railroads of the impossible conditions which were crystallizing as a result of the pre-war policy of regulation.

For these reasons, the Transportation Act, 1920, providing for relinquishment of Federal control, accomplished fundamental changes in the regulation of railroads. It provided for the extension of the regulatory power of the Commission to the farthest point consistent with private or individual initiative and energy. The Commission was given jurisdiction over the issue and the disposition of

*Bulletin No. 4, Rev. General Orders, U. S. R. R. Adm'n., p. 135. Also Senate Hearings, p. 104-6.

the proceeds of securities; over extensions, over the supply of cars and other facilities, over the joint use of terminals and over practically every form of inter-carrier relation, including the question of consolidations in the public interest.*

The system of public regulation begun in 1887 was carried to the point where any further extension of authority would have tended to accomplish the end which the grant of powers conferred upon the Commission was intended to avoid—Government operation.

This extension of power in the logical completion of the process begun in 1887, represents no reversal of statutory theory or policy; *yet its sweeping character necessarily implied an obligation on the part of Congress and its administrative agency, the Commission, to enable the carriers to survive and function on a wholesome basis.* Congress has under this Act attempted to discharge its part of the obligation by the adoption of Section 422, inserting Section 15a in the Interstate Commerce Act.

The House Bill proceeded along the old lines of regulation. The Senate Bill recognized that the history of the administration of the restrictive rate-making provisions of the Commerce Act, the existing status of railway credit and the radical extension of the process of regulation made obligatory the adoption of remedial legislation of the most decisive character if American commerce was to be served and Government ownership avoided. The Senate theory prevailed. It is a

*The far-reaching characteristics of the Act have been adequately described by controlling judicial authority, cited *infra*.

necessary purpose of this brief to discuss as briefly as possible the objective of Section 422 of the Transportation Act [inserting Section 15(a) in the Interstate Commerce Act] and the constitutional theory upon which it is based.

PREVIOUS INADEQUACY OF THE RATE MAKING PROVISIONS OF THE COMMERCE ACT TO AUTHORIZE FULL CONSIDERATION OF THE REVENUE NECESSITIES OF THE CARRIERS

Concurrently with the advance rate cases heard before the Interstate Commerce Commission beginning in 1910, there arose an increasing conviction that the procedure for adjusting rates prescribed by Section 15 of the Interstate Commerce Act was not sufficiently flexible to sustain the American system of transportation or enable it to expand with the high speed necessary to meet the requirements of commerce. The rate-making section of the Commerce Act was written around *the individual rate*. It did not tend to encourage consideration of the effect of these rates in their aggregate upon individual carriers or upon the carriers as a whole. And in those cases in which the railroads had taken steps which were of necessity concerted and in clear violation of the Sherman Act,* to secure contemporaneous advances in

*All that was decided in *Keogh v. C. & N. W. Ry. Co.* 260 U. S. 156, is that the shipper may not under the conditions there stated maintain an action under the Sherman Act for rates initiated in violation of that act but approved by the Commission or otherwise legal under the Commerce Act. On the contrary, the court asserts that "the fact that these rates (that is, rates initiated by concerted action on part of the carriers) had been approved by the Commission, would not, it seems, bar proceedings by the Government."

The history of the difficulties confronting the railroads in the effort to avoid destructive competition—at last placed upon a legal basis only with the adoption of the Transportation Act, which has

their respective competitive rate structures, the procedure and jurisdiction of the Commission came to be widely regarded as unsuited to the necessities of the situation.

Certain members of the Commission had objected to the consideration of the necessity for any general increase in revenue until the proposed ad-

charged the Commission with initial and plenary responsibility for adequate rate structures and with control over minimum as well as maximum rates—is most interesting.

Acting upon the advice of Judge Cooley, given to the carriers shortly after the adoption of the Commerce Act but before the Sherman Act, to the effect that their only protection from destructive competition lay "in the cultivation of reasonable relations among themselves, in mutual forbearance, and the application of a sense of justice to their mutual dealings and in their rivalries" (*C. St. P. & K. C. Ry. Co. Case*, 2 I. C. C. 137), the carriers entered into the traffic agreements which were denounced as illegal as in contravention of the Sherman Act by the Supreme Court in *U. S. v. Trans-Missouri Freight Assn.*, 166 U. S. 290, decided March 22, 1897, and in *U. S. v. Joint Traffic Assn.*, 171 U. S. 505, decided October 24, 1898.

The concerted action necessary to inaugurate any general increase in rates, or, indeed, any inquiry to that end prior to the adoption of Section 15a was confronted by the possibility of injunction, as in 1910, the history of which is narrated in the annual report of the Attorney General for the year ended June 30, 1910, at pages 8 and 9. The history of the main general advance cases before the Interstate Commerce Commission prior to the Transportation Act, 1920, is also set out in the 28th annual report of the Interstate Commerce Commission for 1914.

The obvious illegality of concurrent action by the railroads in simultaneously filing advanced competitive rates is due to the fact that the act of initiation rested with the carrier and not with the Commission or indeed with the filing of the rate. *W. U. T. Co. v. Esteve Bros. & Co.*, 65 L. ed. Adv. Op. 653, 655.

It is a well-known fact that in several of the Advance Rate Cases particular carriers joined in the proceeding to initiate an advance in rates not because of any financial necessity on their part, but out of a regard for their more necessitous competitors. Compare the assertion of one of the carriers at the hearing in the *C., St. P. & K. C. Case* (2 I. C. C. 137): "Our reasons for making rates as above are as follows: At a meeting of the Northwestern Association, of which our line is not a member, but at which we were notified to be present, all the other lines urged us to assent to the rates (the 60-cent scale), which all said lines had adopted. We assented to said rates against our own interests for the sole purpose of assisting our competitors to regulate their local rates in accordance with their necessities, which they alleged to be very pressing."

vances thought necessary by the carriers had been allocated to specified rates or items and filed, for scrutiny as to the reasonableness, *per se*, of the individual increases proposed. *The Five Per Cent Case*, 31 I. C. C. 351, 355.

When the particular increases were thus filed and suspended as a whole for investigation and railway revenue was found to be inadequate there was further vigorous dissent against the subsequent granting of general relief by the Commission, on the ground that the action of the Commission in granting a horizontal increase would constitute "a new and radical departure and a most serious and portentous step, in that by this step the Commission is shown to deem itself justified in sanctioning these increased rates * * * upon consideration of general financial and operating results." 32 I. C. C. 337.

It was further objected that the necessities of the carrier had never been regarded as the test for determining the reasonableness of rates or rate structures; that the sole test is the reasonableness or unreasonableness of each individual rate *per se*.

These objections had some basis in the fact that Section 15 of the Commerce Act was founded primarily on the common law definition of a reasonable individual rate. Each transportation service was regarded by the common law as a separate equation having no necessary legal relation to results in the aggregate or to transportation as a whole; certainly no constructive relation.

The aggregate result might constitute an exces-

sive return upon the present fair value of the property or it might be so inadequate as to destroy the credit of the carriers involved and put an end to the extension of facilities and service; yet until February 28, 1920, the Commerce Act of the United States placed on the Commission little direct responsibility for viewing the problem from any broader standpoint than that of the reasonableness *per se* of individual rates and held out but little encouragement to substitute for the unit process a test based more appropriately on results.

This enforced indifference to net results was exemplified in a number of rate cases.*

In granting partial relief in the *Fifteen Per Cent Case of 1917*, 45 I. C. C. 303, a quorum of the Commission necessary to legal action responded to an appeal of the railroads for emergency relief by consenting to hear the proposal for horizontal increases without prolonged investigation as to specific rates and localities, asserting that investigations of such detailed character were not useful in the exercise of the functions which the Commission was called upon to discharge in determining the reasonableness of proposed rate increases covering the entire country.

The report of the case discloses that this procedure became practicable *only through waivers by the carriers of technical impediments, accom-*

*"A railroad company may be operated with a less return than it ought to enjoy or even at a loss, but neither condition of affairs would justify the exaction by it of rates that are higher than they reasonably should be for services performed, all things being considered." *Railroad Comm. v. Illinois, etc., R. Co.*, 20 I. C. C. 181, 186; *The Five Per Cent Case*, 31 I. C. C. 351, 359. See also *dictum* of Judge Brewer in *Cotting v. Stockyards*, 183 U. S. 79, which six of the Justices declined to follow.

panied by a pledge on their part that if any increases which might be allowed by the Commission were subsequently found by the Commission to be unnecessary they would promptly adjust their schedules accordingly. The necessity for accommodations of that character plainly indicated the lack of flexibility of the Act and the lack of necessary power in the Commission.

Although not satisfied as to the necessity for general relief at the first hearing, the procedure of the Commission in that case undoubtedly evidenced a disposition on part of a majority of its members to approach the matter from the broadest possible standpoint compatible with the statute. Yet it was necessarily recognized (p. 317), that in substance the issue was the reasonableness *per se* of the proposed increased rates rather than the question of the credit of the carriers and their necessity for general relief.

The proper economic basis for the determination of such inquiries was aptly stated by Commissioner Harlan in his opinion dissenting from the action of the majority in restricting the relief granted:

"The record in my judgment demonstrates a proposition that has long been clear to me, namely, that a rate is a public question and that the existing rates, aside from any interest that the owners of our railroads may have in the matter, could well be advanced in the public interest, in order that assurance may thus be given for the early enlargement of our transportation facilities."

The position, however, that the pending issue thus appropriately interpreted by Commissioner Harlan was one exclusively for Congress and not for the Commission to handle was asserted in an opinion by Commissioner McChord in these words:

"The issue presented is in reality one largely of governmental policy, rather than a question whether the rates sought to be made effective July 1 are reasonable for the service of transportation."

So we see that the administration of the Commerce Act was surrounded by formidable doubts as to the extent to which the Commission might give consideration to the underlying factors of credit and net income.

It is needless to suggest that the administration of the Act proceeded with the utmost difficulty under these circumstances and that a part of the membership of the Commission did not feel at liberty to give full consideration to the plain necessities of the carriers upon a hearing restricted to the question of general relief. Initiative was left with the railroads, but under the most embarrassing restrictions and limitations.

CONTROVERSY AND THE INSOLUBLE PROBLEM

A destructive attitude of hostility developed between shippers and railway managements. Class I railway net operating incomes dropped to 4.12 per cent of their aggregate property accounts in 1914, yet nearly two hundred appearances in the *Five Per Cent Case* of 1914 attest the vigorous opposition with which the request for additional revenue was fought. The report of the *Fifteen*

Per Cent Case of 1917 discloses five and one-half pages of protestants against the proposed increase. As a result of the hearings in the general advance cases it became increasingly evident that when the railroads required additional revenue to sustain their credit and the public service, the procedure established by the Commerce Act was unsuited to the rational and dispassionate determination of the question.

Other conditions of the Commerce Act, one procedural and one fundamental, deprived the Commission of necessary discretion and flexibility and proved additional stumbling blocks in the way of adequate relief before the Commission.

The express provisions of the Act placed the burden of proof upon the carriers to justify higher rates. This naturally resulted in a disposition, if not a peremptory duty, on part of the Commission to hold the carriers to a pretty definite discharge of that burden.*

The constructive administration of the Commerce Act was accompanied by a yet more fundamental difficulty, denominated by Senator Cummins during the hearings of the Newlands Committee as the insoluble problem. *The Commission had no power to adjust the competitive rate structure to the circumstances of the different carriers.*

In the first report in the *Five Per Cent Case* of 1914, 31 I. C. C. 351, it was recognized that the

*Thus in the *Fifteen Per Cent Case*, Commissioner Meyer, dissenting from the partial relief granted in that case asserted: "Before important action like this is taken the most conclusive proof of its necessity should be before the Commission," 45 I. C. C. 303, 331; also that the adverse ratios of the available four months of 1917 "do not necessarily predict unfavorable results for the entire year." *Ib.* 334, etc., etc.

net operating income of the carriers in official classification territory, considered as a whole, was smaller than was demanded in the public interest. The Commission said, p. 386, 403:

"Treating as one road the thirty-five railway systems that have joined in this application for our approval of a so-called five per cent advance in their freight charges, ~~we~~ have reached the conclusion that ~~their~~ net operating income is insufficient and should be increased."

General relief in that proceeding was denied, largely because of the Commission's disapproval of the items selected by the carriers for advances. The majority opinion, however, pointed out the disparity in net operating income realized by the various roads and asserted *that the condition of some of the carriers involved was so prosperous "that they clearly do not need a higher net income."* The denial of general relief unquestionably left many of the carriers with inadequate revenue. In like manner the denial of relief in 1917 was based in part upon the proposition that the admitted necessities of certain roads cannot justify a course of action that is unwarranted by the condition of the larger number of strong and successful lines.

It may be that no complaint of this situation is justified from the standpoint of the investors in the securities of the less fortunate railroad. They take the ordinary chances of competition and commercial disaster. *But the service of the public dependent upon these lines is a different matter;* and no system of regulation under the commerce

clause can be regarded as statesmanlike which fails to make an effort to stabilize credit and returns by adjusting the general rate structure to the necessities of the different carriers. No such effort was discernible in the Commerce Act.

RAILWAY CREDIT AND REVENUE THE PROBLEM BEFORE CONGRESS

The Commission had neither the power nor the responsibility necessary to avert a gradual breakdown in credit without evading the procedure contemplated by the Commerce Act or without producing revenue for certain carriers in each competitive territory which would have been so excessive as to impair the Commission's standing before a public not likely to understand the difficulty. Forced to choose between excessive revenue for certain roads and inadequate revenue for others, it followed the latter course in the first reports in those hearings brought on by the carriers in unavoidable violation of the Sherman Act. No better result was attained by the railroads themselves during the period in which rate initiative had rested with the managements. They were tied hand and foot with repressive legislation—State and Federal.

The impossibility of sound rate adjustments under the Commerce Act is well illustrated by the disparity in earnings experienced by Class I railroads under Federal operation. We find that during 1919 the Union Pacific earned 139.9 per cent of its standard rental, while the average for the Central Western Region was only 88.6 per cent. The Richmond, Fredericksburg & Potomac earned

243.1 per cent of its standard rental, while the average for the Southern Region was 52.9 per cent. These illustrations suffice to show that any general advance of competitive rates necessary to enable carriers indispensable to the public service to survive would have tended to produce excessive income for certain favorably situated carriers without the application of any additional energy or service on their part.

From this it results that the adequate regulation of railways under competitive private ownership required that broad powers of rate adjustment be given the Commission through the power to initiate rates and to control divisions of rates, etc., and that excessive disparity in results which might remain notwithstanding the exercise of a fair discretion in these respects, constituting a by-product of rate levels necessary to sustain transportation as a whole, should be further leveled by a fair regulation of excess earnings in the public interest.

All of this amounts merely to the rational adjustment of the rate structure to the circumstances (and the constitutional and reasonable demands) of the various carriers. The Commerce Act was wholly lacking in these fundamentals.

Under these inflexible conditions inadequate revenue from time to time and gradual disintegration of railway credit were inevitable.

The limitations and difficulties of regulation under the Commerce Act, because of the secondary aspect of revenue considerations and inability to adjust the rate structure, etc., will be graphically understood from a review of some of the more im-

portant proceedings before the Commission, among which may be cited: *In re Proposed Advances in Freight Rates*, 9 I. C. C. 382, 404; *Eastern Advance Rate Case*, 20 I. C. C. 243, 261; *Five Per Cent Case*, 31 I. C. C. 351; 32 I. C. C. 329, 337, 340, in which this pregnant suggestion was made by Commissioner Clements in the face of the problem found insoluble until the adoption of Section 15a:

"It is by no means certain that it would not, in the long run, be cheaper to the public to guarantee the bonds of the weak roads unable to meet their obligations rather than to try to take care of them by increased rates, which inure to the strong roads as well as to the weak."

And see 45 I. C. C. 303, 311, 331.

Surely no such alternative is necessary until Congress has fairly exhausted its efforts at constructive regulation and conservation under the Commerce Clause.

It was largely to meet these conditions that Congress adopted the Transportation Act of 1920. Failure to recognize these basic economic considerations to which Congress plainly reacted will result in a complete inability to visualize the purpose and intent or the economic or constitutional basis of that constructive measure.

May we have the further indulgence of Your Honors while we point out the historic steps by which Congress arrived at its conclusions?

**INTENSIVE RE-SURVEY BY CONGRESS OF THE ENTIRE
RAILWAY PROBLEM RESULTING IN TRANS-
PORTATION ACT, 1920**

Resulting from the considerations above mentioned and concurrently with their demonstration in the advance rate hearings beginning in 1910, there arose an increasing conviction that the restrictive and controversial basis of Section 15 of the Commerce Act prevented the Commission from viewing transportation as a whole or else from giving effect to its constructive conclusions. This thought was given official sanction in the message of the President of the United States, to be found in the Congressional Record for December 7, 1915 (p. 99), in which it was recognized that the transportation problem was an exceedingly pressing one. Congress was urged "to provide for a commission of inquiry to ascertain by a thorough canvass of the whole question whether our laws as at present framed and administered are as serviceable as they might be in the solution of the problem."

This message was appropriately interpreted by Senator Underwood as referring to the necessity for legislation to strengthen railway credit in order to avoid a breakdown of the transportation system. He asserted that the question was whether we were to avoid the next step—Government ownership—and whether the American people were willing to put up with an unsafe, inferior and inadequate transportation system, or have the intelligence to pay for one that would supply their needs. Cong. Record, Feb. 22, 1916, p. 3421. The Joint Committee, appointed in July

1916, to investigate the problem pursuant to the President's message and the Newlands (Underwood) Resolution, functioned until its duties were superseded by the war and Federal control. The Senate and House Committees took up the work where it was left off by the Joint Committee. The Transportation Act, 1920, approved February 28, 1920, is the direct result.

Before proceeding with the theory and purpose of that part of the Transportation Act directly involved in this proceeding (Section 15a), it should be pointed out that two of the other important departures accomplished by the Transportation Act in the effort of Congress to sustain by constructive regulation the agencies of transportation as a whole, have been reviewed and upheld and the radical transformation in regulatory theory worked by the Transportation Act have been observed and approved. First and most important is the decision in the *Wisconsin Passenger Fare Case*, 257 U. S. 563, in which was recognized the intention of Congress that the *revenue necessities* of the carrier should be regarded as a fundamental purpose of the Transportation Act and that these necessities could not be protected unless burdensome State rate structures were harmonized with the interstate rate structures; and that the regulation of railway transportation was for the first time by the Transportation Act placed on a truly national and constructive basis.*

*See also the *New York Passenger Fare Case*, 257 U. S. 591; *State of Texas v. I. C. C.*, *supra*.

As stated by Chief Justice Taft in the *Wisconsin Case*, the Act constituted a "new departure" imposing "an affirmative duty on the Interstate Commerce Commission to fix rates and to take other important steps to maintain an adequate railway service for the people of the United States."

Of primary importance also is the *New England Divisions Case*, 261 U. S., 184.

Congress unquestionably sought to make effective, and as nearly automatic as possible, the administrative reaction of the Commission to the revenue necessities of the carriers as units of our general system of transportation and for the first time conferred upon the Commission the power to adjust the rate structure to the legitimate (and constitutional) requirements of the individual carriers while at the same time dealing with the carriers as a whole, or by groups, as the Commission might find necessary. On this basis and for this purpose the principle of grouping and of group rate-making and of group valuation was provided. This provision, with its necessary corollary, the recapture clause of Section 15(a), became, as heretofore suggested, the storm center around which controversy was waged before Congress during the formulation of the Transportation Act. It was adopted because Congress recognized that under no other condition could be justified a mandate to the Commission, more or less automatic in its nature, that would produce (the economic situation permitting) adequate revenue *and result, in the absence of the recapture clause, in unregulated excess earnings which would of necessity be produced in case of particular carriers if the rate level were pitched on a plane that would sustain the agencies of the transportation as a whole within each group.*

THE GROUP BASIS FOR GENERAL RATE ADJUSTMENTS

Before discussing in detail its constitutionality it may assist to state in the margin concisely the

effect of that part of the statute which precedes the recapture clause, viz.: the mandate that the Commission shall from time to time initiate on its own responsibility and maintain rates that will produce a fair aggregate return, under honest and economic management, upon the fair aggregate value of the railway property devoted to the transportation service.*

Grouping of carriers is contemplated for the more accurate and convenient execution of this duty. From the standpoint of administrative mechanism and public confidence grouping would seem essential, but whether embraced in one national group or in the familiar classification territories or otherwise, it would be incumbent upon the Commission to scrutinize the effect of rates upon the different carriers in order to see that the rate adjustments put into effect by the Commission were not unduly concentrated or monopolized.

The radical change lies in the direct mandate to the Commission to initiate and maintain rates that will enable the carriers as a whole or in the different competitive groups defined by the Commission to earn a fair ratio of return upon the aggregate value of the transportation machine in each group. After two years this fair ratio of return was to be ascertained and declared from

*This does not assure returns to individual carriers on any definite basis. It treats the railroads as a whole, or in such groups as the Commission may establish, as a single transportation machine which, in order to survive, must be enabled to earn a living return on its fair total value. What portion of the gross revenue each road will receive and earn from the rates pitched on this basis is left dependent upon ordinary considerations of location, competition and efficiency—subject to a limited but constructive power on part of the Commission to equalize inadequate revenue in the public interest through control of divisions and through the adjustment of local or non-competitive rates.

time to time by the Commission.* It must, first of all, be a fair rate of return on aggregate railway value, and in arriving at the rate the Commission must give adequate consideration to the transportation needs of the country and the necessity for the continual enlargement of transportation facilities in the public interest.

Adequate railway revenue is no longer even primarily a private matter. While changes in rates by carriers under Section 15 of the Commerce Act are on the old basis, the initiation of rates by the Commission is a new power pitched on a public basis and embraces control over the general level or relationship to general revenue of intrastate as well as interstate rates. State authorities proceed as heretofore in the adjustment of local rates, but must proceed in substantial harmony with interstate rate levels or adjustments established from time to time by the Commission under Section 422 of the Transportation Act. Hence responsibility in gross and in detail rests upon the threshold of the Interstate Commerce Commission, the national agency, a fact which has a definite legal bearing

*It has been placed at the 5% level in the hearing entitled *Reduced Rates, 1922* (No. 13293), 68 I. C. C. 676. The carriers recognize that economic conditions—and the law of diminishing returns—set limits upon railway revenue which can not be ignored. It is plain, from a practical standpoint and therefore from the standpoint of the Constitution, which does not ignore practical considerations, that rates could not be raised to a level that would increase the group return from the subnormal levels of 1919 (2.36%), 1920 (.08%) and 1921 (2.95%) to a full 6, 7, or 8% for the group without throttling commerce. The Commission has, accordingly, proceeded slowly and the carriers have demonstrated their faith in the constructive attitude of the Commission by acquiescing in the announced objective of 5% as the group ratio. Of course, if commerce will stand a better return, it is not to be doubted that it will be announced and made effective by the Commission to give effect to the wholesome and constructive purpose of Congress.

upon the right of Congress to regulate excess revenue, from whatever carrier source derived, produced under the new system of regulation.

**THE ARGUMENT AGAINST THE RE-CAPTURE CLAUSE
OVERLOOKS THE FACT THAT IT IS MERELY AN EF-
FECTIVE PROVISION FOR THE ADJUSTMENT OF
THE RATE STRUCTURE TO THE CIRCUM-
STANCES OF THE INDIVIDUAL CARRIERS**

The chief objection used against the provision both before Congress and in the present proceeding has been based upon the assumption that earnings are to be levelled by a retrospective act of seizure of earnings already received unconditionally by carriers, as a result of the application of rates declared by proper authority to be just and reasonable, and, therefore, lawful and final for all purposes. That conception of the process is erroneous.

The statute, as adopted, asserts in substance that in order to sustain competitive transportation as a whole, rates may have to be established which are intentionally higher than necessary to satisfy the private rights of sundry individual carriers, or to the discharge of their public duties. To the extent that the rates received by any carrier reflect an excess over a fair return upon its property, they are accordingly declared to be received tentatively and in trust for a transportation fund to be administered in furtherance of the public interest in transportation.

An analytical statement of the provision answers most of the objections which have been directed against it. Thus, in his letter dated September 19, 1919, referred to above, questioning

the constitutionality of that provision relating to the disposition of excess earnings as embodied in the original draft of the Cummins Bill (Senate 2906), Mr. Hughes bases his objections primarily on the criticism that, since the section provides that rates must be just and reasonable, they are therefore lawful, and that the provision for the recovery of any part of the earnings resulting from such lawful rates appears to be nothing more than a taking of property by the Government contrary to the Fifth Amendment.

His exact statement of the situation, as he saw it, is:

"If, however, the rates thus fixed, charged and received by a carrier are to be deemed just and reasonable for the services rendered, the carrier is entitled to these receipts as its property, and the taking by the Government of any portion of these receipts (except under a valid tax) for general Governmental purposes or for the benefit of other carriers would appear to be a taking of property contrary to the Fifth Amendment to the Federal Constitution."

We have already seen that a correct understanding and analysis of the process of excess earnings regulation is impossible unless it be clearly borne in mind that these rates, while final so far as the shipper is concerned, are specifically impressed with a trust when and as received by each carrier, to the extent that they may produce in the aggregate an excess over a reasonable return upon the property of the carrier held or used for the service of the transportation.

RATES ADJUSTED TO GROUP REQUIREMENTS

It is erroneous to conclude that they are just and reasonable for every carrier to retain merely because Congress has established them for the shipper to pay. They are to be established not for any particular carrier or for any specific service by any particular carrier. They are to be adjusted to a level necessary to sustain transportation in the aggregate or in the group. They are not, as erroneously assumed by Mr. Hughes, "deemed just and reasonable for the services rendered." On the contrary, they are expressly declared by the statute to be necessarily *in excess of what is just and reasonable* for the service rendered by particular carriers. They are nevertheless just and reasonable as a uniform rate for all shippers to pay, as it is obviously just and reasonable for the shipper to pay whatever is necessary to keep alive the essential agencies of transportation in competitive areas; but that is very different from the assumption that rates made on a group or aggregate basis have been declared to be "just and reasonable" as to every carrier and every service, or as to every shipper.

Any such conclusion rests upon the hypothesis that Congress must perpetuate that discredited method of establishing rates which is based exclusively on the cost or value of *each particular service*. Neither cost nor value of each service is capable of satisfactory proof. The cost varies with every shipment and with every carrier. The value of the service is different for every shipper. So in adopting the test of results in the aggregate as a material factor for the adjustment of rates,

Congress will be adopting, as far as it is practicable to apply the measure to groups of competitive carriers, the service at cost basis, determined by results in the aggregate, so widely employed in the case of local utilities. It is the final test uniformly applied by the courts in determining the reasonableness of rates as a whole and is a process squarely within the purview of the commerce clause. Bear in mind the established fact that:

"Where the rates as a whole are under consideration there is a possibility of deciding, with more or less certainty, whether the total earnings afford a reasonable return." *I. C. C. v. P. R. R. Co.*, 222 U. S. 541.

Is Congress foreclosed from employing the more accurate mechanism?

RATES MAY BE TENTATIVE OR CONDITIONAL

The contention is then made that some of these rates may have been established in proceedings to test the reasonableness of specific rates, such as under Section 15 of the "Act to Regulate Commerce," and that surely rates so established cannot be regarded as carrying any excess—particularly where they happen to be non-competitive rates. *A complete answer to this suggestion is that Congress may undoubtedly make rates for the future for any carrier based on the best available data with the hope that the rate structure thus guessed at will produce a reasonable return, or it may permit rates which are relatively just and free from discrimination but which, so far as*

the carrier is concerned, are tentative and subject to the test of actual results. The former is prophetic and uncertain. The latter is absolute in its accuracy.

Is Congress to be denied the right to employ an absolute measure or a combination of the two methods because in the past it has employed, with unscientific and unsatisfactory results, the inaccurate method of prophecy? We find nothing in the commerce clause to warrant any such limitation and as long as specific commodities or integral railway services are not singled out for discriminatory action the carrier cannot complain of appropriate methods of rate regulation where a fair and reasonable return in the aggregate is assured to the carrier complaining.

**MODIFICATION OF SHIPPERS' SO-CALLED COMMON LAW
RIGHT TO DESTRUCTIVE COMPETITION OR TO A
RATE STRUCTURE THAT WOULD DESTROY
COMPETITIVE CARRIERS**

The criticism next seems to switch from the complaint of the carrier to a complaint on behalf of the shipper who would be unlawfully compelled, so it is said, to pay in rates the "unreasonable" excess to be recovered from any given carrier. Thus, as asserted by Mr. Hughes:

"On the hypothesis that the charges are unreasonable, the power to authorize them, no less than the power to collect them, falls. The exaction and maintenance of such charges would deprive shippers and passengers of their property without due process of law."

Of course, the carrier could not complain on

that ground. *I. C. C. v. C. R. I. & P. R. Co.*, 218 U. S. 88, 109; *A. T. & S. F. R. Co. v. U. S.*, 232 U. S. 199; and cases cited.

This suggestion also loses sight of the fact that rates may properly be made on a group basis. Of what "property" is a shipper being deprived when he is asked to pay rates that will produce a fair return on the aggregate railway property in any rate-making district? He has no constitutional right to insist that Congress shall make different rates for each carrier. He has no right to complain that rates are made with reference to aggregate or average conditions. He certainly has no right, superior to the commerce clause, to demand that Congress shall permit essential agencies of transportation to be destroyed through competition in rates. In suggesting the contrary the learned jurist, Mr. Hughes, overlooked an established practice by the Commission inconsistent with his views. *Spokane Case*, 15 I. C. C. 376, 392; *Eastern Advance Rate Case*, 20 I. C. C. 243, 273, 274; *Kindel Case*, 15 I. C. C. 555; 9 I. C. C. 382.

Congress has by this Act* almost completely suppressed competition in rates as being destructive of the carriers' ability to perform their public functions. And Congress has the undoubted power under the commerce clause to establish and enforce uniform rates in competitive areas that

* . . . giving the Commission jurisdiction over minimum as well as maximum rates and putting a final end to destructive competition (*Keogh v. C. & N. W.*, 260 U. S. 156) a power lacking in the Act as construed at an early date in its history. *C., St. P. & K. C. Ry. Co. Case*, 2 I. C. C. 137; *I. C. C. v. C., N. O. & T. P.*, 167 U. S. 479.

will produce an "unreasonable" return to certain carriers, if that process is necessary to sustain essential competitive lines. That excess cannot be repaid to the shipper. It would then constitute a rebate (exactly as observed in the *Keogh Case*, cited in the footnote) that would attract all competitive traffic and defeat the main objective, which is the survival of existing necessary agencies of transportation.

RAILROADS MUST SURVIVE BEFORE THEY CAN BE
FORCED TO COMPETE

The right of a shipper to have his commodities transported by each common carrier at a reasonable rate for each service, whatever that may mean if it implies anything contrary to the theory of the Transportation Act, is a mere common law right that is as much subject to the discretion of Congress under the commerce clause as was the common law right of carriers to pool their tonnage, to combine or to enforce the fellow-servant doctrine as to their employees. It was never a property right or a right protected against modification by Congress under the commerce clause. Many of the common law rights of carriers have been abrogated in order to enforce a competitive status among competing carriers. They must survive before they can compete. Any rate regulation found necessary by Congress to enable them to survive cannot be "unreasonable" from a constitutional or any other standpoint, and we have never understood that the legislation of Congress or its results must be found by the courts to be reasonable if it is appropriate and within the

scope of any of the powers delegated by the Constitution and does not run counter to some express constitutional limitation.

We touch this subject again at a later point in this brief at the risk of some repetition, but the question is too fundamental to warrant confusion. There has been so much misapprehension about the application of the maxim that rates must be reasonable to the shipper, that we set out in the margin the sound observations made in *Brunswick & T. Water District v. Maine Water Co.*, 99 Me. 371, 59 Atl. 537, dealing with the immediate question of rates of a local utility supplying water to the public, but making plain that the slogan "*reasonable rate to the shipper*" means that the rate must be a reasonable rate for the public generally, not for the particular customer, and this means a rate reasonable for the public to pay to reproduce and sustain the service by the competitive agencies which the public policy of the United States demands in railway transportation.*

*The Court said " * * * We do not doubt that when the worth of a public service of this kind to the public or the customer is spoken of necessarily one of the elements to be considered is the expense at which the public or customers, as a community, might serve themselves were they free to do so. * * * When the worth of water to a consumer is to be estimated, we are not limited to the value of water in itself, for it is an absolute necessity. Its value has no limit. * * * In estimating what it is reasonable to charge for a water service, that is, not exceeding its worth to the consumer, water is to be regarded as a product, and the cost at which it can be produced or distributed is an important element in its worth. It is not the only element, however. The individuals of a community may with reason prefer to pay rates which yield a return to the money of other people, higher than the event shows they could serve themselves for, rather than make the venture themselves, and risk their own money to loss in an uncertain enterprise. It was said by us in the Waterville case that the investor is entitled to something for the risk he takes, and it is not unreasonable for the consumer to be charged something on that account. That is one of the things which make up the worth of the water to the customer. The same

The case cited is, we think, mistakenly criticized by Judge Prouty in *Eastern Advance Rate Case*, 20 I. C. C. 243, 273, 274, as being too restrictive upon the utility, since he considered that if the doctrine there stated were applied to competing railroads it would force the road having higher costs between competitive points to come down to the lower cost of its competitor. This does not follow under a sound system of regulation. The "community" or "public" whose interests form the criterion in such cases is *the general public*—and not the interest of an individual shipper or any of given community. In the case of interstate commerce the public interest involved is as broad as the commerce clause, and under the Transportation Act the public interest involved in any given inquiry is the national public or the public served by any group into which the carriers may be divided for rate-making purposes by the Commission, that is, a public served by *all of the roads*.

ADAPTATION OF RATE STRUCTURE TO THE RESPECTIVE CARRIERS AND THE PRINCIPLE OF CLASSIFICATION

It is in effect contended that Congress must finally establish the same rate for a railroad which hauls one bale of hay between two given points as it establishes for another railroad hauling a million bales between the same or compa-

element enters always into the relation between producer and consumer. * * *

"In the aspect now being considered, the worth of a water service to its customers does not mean what it would cost some one individual, or some few individuals to supply themselves, for we may be blessed with a spring and another may have a good well. *It means the worth to the individuals in a community taken as a whole. It is the worth to the customers as individuals, but as individuals making up a community of water takers.*"

able points, and that some constitutional right is violated if Congress or the rate-making authorities give adequate consideration to the factors of density or cost. It is perfectly obvious that any such contention is ill-founded. The common law imposes no such requirement. The spirit of the commerce clause affirmatively forbids any such destructive conclusion.

All railroads are not entitled as a matter of law to the same return for a like general service, *I. C. C. v. Union Pac. R. Co.*, 222 U. S. 541. In the *Covington Turnpike Case*, 164 U. S. 578, it was asserted that a road could afford to charge less toll by reason of dense traffic upon it than roads where the traffic was not so dense and that the legislative authority might appropriately recognize the distinction. Is it not clear that Congress may employ any appropriate method in order to give effect to the recognition of such distinction?

It may well be that Congress may desire the same rate charged for the same class of service; that is, equality in rates, so far as the shippers and passengers are concerned and in order to avoid discrimination (*Seaboard Air Line v. Florida*, 203 U. S. 261, 269); but this is fundamentally different from the assertion of that policy by a carrier in its own right.

The United States Supreme Court has always approved the propriety of classifying railroads according to their earning power, per mile or as a system, for the purpose of determining rates. Thus, in *Chicago, etc., R. Co. v. Iowa*, 94 U. S. 155, a classification was held to be reasonable and proper which divided the railroads into classes

according to gross earnings per mile and permitted the different classes to charge different rates. That principle is now embodied in many rate statutes.* In the case last cited the Court said:

"It is very clear that a uniform rate of charges for all railroad companies in the State might operate unjustly upon some. *It was proper, therefore, to provide in some way for an adaptation of the rates to the circumstances of the different roads*; and the general assembly in the exercise of its legislative discretion has seen fit to do this by a system of classification."

That is, in its last analysis, exactly what is accomplished by the provision objected to.

Confronted with the necessity that competitive rates must be uniform, Congress cannot adapt these rates to the circumstances of sundry carriers by making them unequal. The low rate would attract all of the business and destroy the competitor. Hence the only available process is to make the rates tentative so far as the carrier is concerned, subject to the test of aggregate result. It is a simple and effective adaptation of a rate fabric to the varying circumstances of individual carriers and squarely within the principle announced by the Supreme Court.

In *Dow v. Beidelman*, 125 U. S. 680, the court sustained a statute which fixed passenger rates at from three to eight cents per mile, *according to*

*For example it formed the basis of the Alabama statutes (that is, a classification according to earnings) for rate regulation set out in the Code of 1907, Section 5566. *R. R. Com. of Ala. v. Cent. of G. R. Co.*, 170 Fed. C. C. A.) 225.

the length of the road, approving Chicago, etc., R. Co. v. Iowa, supra.

In *Chicago, etc., R. Co. v. Wellman*, 143 U. S. 339, the court sustained the Michigan statute which fixes the passenger fares according to gross earnings per mile.

Other notable instances of classification along lines analogous to that employed in the Act are discussed in the following cases: *Ames v. Union Pacific*, 64 Fed. 165; *Houston, etc., R. Co. v. Storey*, 149 Fed. 499; *Commissioner v. Wabash R. Co.*, 123 Mich. 669, 82 N. W. 526. See note, 21 Ann. Cas. 191; 14 Rose's Notes 222.

The criticism referred to asserts that the process of regulating rates according to the result of those rates "confuses the Government's power over rates with an asserted governmental power over the amount of net earnings from lawful rates."

The error in that assertion is twofold. It assumes that rates may not be fixed tentatively and subject to the test of actual results, and that because they are made lawful they are necessarily final for all purposes.

If it were necessary to sustain the provisions relating to the disposition of excess earnings, it is demonstrable that these provisions are in effect merely a regulation of the individual rates collectable by the various carriers, worked out through a classification in accordance with the principle sustained in the cases above cited.

SCOPE OF COMMERCE CLAUSE

But it is not necessary to restrict the inquiry to such narrow compass. The commerce clause is

not a mere police power restricting Congress to a check upon individual rates, although it undoubtedly confers upon Congress as complete authority over individual interstate rates as is reserved to the several States over local rates in the assertion of their police jurisdiction.

The power to regulate commerce includes the power to adopt all appropriate processes to sustain the movement of commerce and preserve the essential competitive agencies through which commerce between the States is conducted. So long as individual carriers are not prevented by the legislation, as distinguished from the risks of the venture, from earning a fair return upon their property devoted to the public service, they cannot complain if Congress prefers to deal with rates in the aggregate rather than with each unit of service. It has long since become obvious to those observers who have remained open-minded upon the subject that commerce cannot be regulated in the public interest if Congress restricts its program of rate regulation to the unit measure basis.

The only limitation upon the legislative authority is that the regulation of rates, whether by units or in the aggregate, shall not prohibit the earning of a reasonable return upon the property employed in the public service. The power of regulation may be exerted to that *limit* by any appropriate process.

PRINCIPLE NOT NOVEL

The process of regarding results as the test or the limit for rates is not novel. That test was

among the earliest applied to American railroads, many of which began their existence with a charter limitation upon net income (Laws, New York 1828, chap. 304, p. 13). Judge Hughes cited nine similar statutes as a common form of early rate or earning restrictions in the opinion in the *Minnesota Rate Cases*, 230 U. S. 352, 454.

Until opposition was precipitated against this proposal, it had not been seriously contended since the decisions of the Supreme Court in the *Granger Cases* in 1874 that railroads have a right to realize or retain unlimited earnings or to net railway operating income in excess of a reasonable return upon the value of their property.

The State of Tennessee adopted a statute in 1883 providing for the punishment of any railroad which took, in rates, more than a "fair and just return" on its investment, *L. & N. R. Co. v. R. R. Com.*, 19 Fed. 679, 691-2. The Federal court declared the statute invalid, not because the legislature was without authority to restrict income to a fair and reasonable ratio of return, but because the statute failed to prescribe with the certainty necessary in a penal statute what was considered by the lawmakers to be a fair and just return which the railroad must observe. Of course, Section 15a avoids this difficulty (*Rent Cases*, cited 258 U. S. 242, 250, *supra*) which the *Lever Act* prosecutions did not avoid. (See footnote, pages 6 and 7, *supra*.)

The result of rates, as it was one of the first tests applied, is also one of the most recent. This fact is repeatedly illustrated in the ordinances

and agreements with street car lines and local utilities whose rates are in many cases tested and automatically adjusted according to results.

FUNDAMENTAL PRINCIPLES PLAINLY SUSTAINING
CONSTITUTIONALITY OF SECTION 15a

So much misconception of the process is due to vague constitutional theories invoked whenever the legislative authority finds it indispensable in the public interest to make novel applications of well settled powers, that a running summary of the controlling decisions is desirable.

(1) A carrier which has devoted its property to public use is entitled to demand no return in excess of a fair return upon the reasonable value of the property at the time it is being used for the public, *Smyth v. Ames*, 169 U. S. 466; *Covington, etc., Turnpike v. Sanford*, 164 U. S. 578; *Wilcox v. Consolidated Gas Co.*, 212 U. S. 19.

(2) Rates on particular commodities must not be confiscatory, but if particular or special rates yield a reasonable compensation, adequate total return is all that the carrier is entitled to demand, *Northern Pacific v. North Dakota*, 236 U. S. 585; *Wilcox v. Consolidated Gas Co.*, 212 U. S. 19; and in providing for a constitutional return the right of the public to be charged only what is reasonable and just for the service is a primary consideration, *Covington, etc., Turnpike v. Sanford, supra*. The Transportation Act recognizes that this last mentioned criterion is one for the benefit of the public which may be waived or modified by public authority; and that, if pressed inexorably, it may "kill the goose." The Act therefore asserts as the

fundamental basis of the new program that it is reasonable for the public to pay whatever is necessary to produce a reasonable return under honest and efficient management upon the aggregate value of the railway systems. We have fully discussed this so-called "shippers' right" which Mr. Hughes advanced against this policy and found that the term "shipper" merely refers to the public at large, whose rights are paramount over merely local or individual considerations, in the determination of a transportation policy.

(3) In pursuance of its wise objective, the systems of transportation are accepted by the Act as they stand. Their construction was permitted by the law-making authority. Whether originally justified or not communities dependent upon their service have grown up within their curtilage. So the Transportation Act properly takes hold of the greatest transportation machine in the world, as it now exists. Wasteful and improvident construction in the future is amply provided against by the sweeping control given the Commission over security issues and new construction.

(4) The Supreme Court repeatedly asserted, at the time of the original decision in *Munn v. Illinois*, 94 U. S. 113, that "where property has been clothed with a public interest, the Legislature may fix a limit to that which shall in law be reasonable for its use." It was originally held that this limit, when fixed by the Legislature, binds the courts as well as the public, *Peik v. Chicago, etc., R. Co.*, 94 U. S. 164; *Chicago, etc., R. Co. v. Iowa*, 94 U. S. 155. This latter expression was, of course, cor-

rected in the latter cases, *Stone v. Farmers, etc., Co.*, 116 U. S. 307; *Georgia, etc., R. Co. v. Smith*, 128 U. S. 174; *Chicago, etc., R. Co. v. Minnesota*, 134 U. S. 418; and *Chicago, etc., R. Co. v. Wellman*, 143 U. S. 339, in which the principle was recognized that the right of "regulation" does not carry the power to destroy, and that the question of reasonable return on the property is, in its final analysis and subject to a broad legislative discretion, for the courts to determine as a matter of fact and not for the legislature as a question of policy or expediency; but the court has never abandoned the proposition that the power of regulation may be exerted to limit the carrier to a reasonable return upon its property employed in the public use. That formula was expressly asserted in *Smyth v. Ames*, 169 U. S. 466, and remains the final expression of the court, reaffirmed in a multitude of decisions, which may be found cited in the margin in *Northern Pac. R. Co. v. North Dakota*, *supra*, at p. 600, and concluding with the *Galveston Case*, 258 U. S. 388, the *Houston Case*, 259 U. S. 318, and the *New York Gas Case*, 258 U. S. 165; and later decisions.

The corollary to the general principle, above referred to, may restrict the carrier to net earnings amounting to less than what would, abstractly considered, be a fair return on its property investment, but that is a risk which the carrier assumes and is thoroughly established, *Covington Turnpike Case*, *supra*; *Interstate C. C. v. U. P. R. Co.*, 222 U. S. 541; *Northern Pac. R. Co. v. North Dakota*,

supra. The carrier fortunate enough to earn more than a fair return cannot complain if Congress elects either permanently or conditionally to waive any limitation upon its charges until definitely assured that the carrier will earn a fair return.

(5) It is obvious that the question what is a reasonable charge for each service is not capable of exact answer. The answer is always at best an approximation. It is almost invariably determined by the relation of the rate under analysis to other rates or established precedents or base rates.

On the other hand, the question of a fair return in the aggregate is a fairly easy question where, as under the Transportation Act, no necessity of separating interstate and intrastate earnings is involved (*Wisconsin Passenger Fare Case*). Hence, any argument that Congress cannot use aggregate return as a test, but must confine itself to the unit measure, would, if sound, prevent Congress from using the accurate and adequate test and force it to employ the admittedly erroneous and approximate unit measure, in which the chances for error increase inversely with the size of the unit and the entire process is a guess into the future.

No doubt is to be entertained of the fact that each carrier is entitled to impose a reasonable charge for each service performed, when all shipments of any given class of commodities or under any rate are to be considered. This has been too frequently stated to be a matter for serious con-

troversy. Thus in *Interstate C. C. v. U. P. R. Co.*, *supra*, it was aserted by Justice Lamar that the fact that the carrier's total income enables it to declare dividends would not justify an order requiring it to haul any particular commodity for less than a reasonable rate; but in that case the court very properly distinguished between proceedings involving a particular rate and *proceedings involving the rates as a whole* and asserted that "where the rates as a whole are under consideration, there is a possibility of deciding, with more or less certainty, whether the total earnings afford a reasonable return"; and this distinction was clearly recognized in *Northern Pac. R. Co. v. North Dakota*, *supra*, where the court said: "When the question is as to the profitableness of the intrastate business as a whole under a general scheme of rates, the carrier must satisfactorily prove the fair value of the property employed in its intrastate business, and show that it has been denied a fair return on that value."

In short, the carriers may, in determining the question of constitutional return apply the gross test, with its stated limitations, and there is no sound reason why the Government may not employ a like measure in checking results for the purpose of regulation.

(6) The test, as to the limit of the police power of a State, as said by Justice Hughes in the *North Dakota Case*, *supra*, is dual and reciprocal; the railroad can deny the right of the regulatory authority to single out and require it to haul any class of commodities at a loss, and the rate-mak-

ing power can restrict the railroad's total net revenue to a reasonable return; but, conceding that the railroad is not forced to haul commodities covered by any given rate for less than is a fair rate to be charged for the service or less than is compensatory to some extent, the railroad cannot complain of confiscation if its aggregate return upon the property investment is reasonable.

If these considerations apply to regulation under the police power of the several States, is it not clear that the power to regulate commerce, vested in the general government by the Constitution, not only runs parallel with the police power reserved to the States over local rates but embraces all possible methods and processes having a direct relation to that end and deemed appropriate by Congress, provided the result is not in conflict with the Fifth Amendment?

FLEXIBILITY IN SOUND REGULATION

It has been shown that there is no merit in the contention that all railroads are entitled, as a matter of law, to the same interstate rate for a like general service under all circumstances. The contrary is frequently noted. Conditions are never identical, and *paramount over all criticism of that character is the commerce clause, which permits all rational regulation that does not reduce the earnings of the carrier below a reasonable return, is necessary to insure competition in service or other sound policy of regulation, and is based on other tangible and substantial requirements or classifications appropriate to the regulation of interstate commerce.*

Under Proposition XIV are stated analogous exertions by the courts of mechanism and practices found convenient in the administration of justice, such as the principle of impounding revenue pending a test of rates or pending a hearing and the more remote but quite analogous trust fund illustration. They present cursory illustrations of the expedients adopted by the courts in aid of a lawful objective which are not to be considered as beyond the power of Congress in dealing with the most difficult, the most complex, of all internal problems and the one affected with the widest public interest. It is manifest that the widest flexibility in treatment is necessary and no doubt should remain as to the power and discretion of Congress under the oft repeated doctrine declared by Chief Justice Marshall in *McCulloch v. Maryland*, 4 Wheat, 316, 421, constituting the most impressive of the great maxims which have come thundering down from his generation to our own:

"We admit, as all must admit, that the powers of the Government are limited, and that its limits are not to be transcended. But we think the sound construction of the Constitution must allow to the national legislature that discretion, with respect to the means by which the powers it confers are to be carried into execution, which will enable that body to perform the high duties assigned to it, in the manner most beneficial to the people. Let the end be legitimate, let it be within the scope of the Constitution, and all means which are appropriate, which are plainly adapted

to that end, which are not prohibited, but consist with the letter and spirit of the Constitution, are constitutional."

Before concluding, we shall revert to the question of the so-called right of the shipper—not because the carrier can assert it, but because it presents the only inquiry in connection with the theory of Section 15a which may properly be said to call for economic justification, since it is in the last analysis the shipper (and passenger) who pay the excess recovered in part from the carrier.

**FURTHER ANALOGIES AND FINAL OBSERVATIONS AND
SUMMARY AS TO THE SHIPPER AND THE ECONOMIC
JUSTIFICATION FOR THE CREATION OF THE
EXCESS EARNING IN THE FIRST INSTANCE**

The shipper's general remedy for specific overcharge is not proposed to be changed by the Act [Section 15a (17)], and no possible constitutional right of the shipper is infringed by the proposed process of excess earnings reduction.

The shipper has, unless and until changed by Congress in the general welfare, a common law right to have his commodities transported at a reasonable rate, but, as we have seen, that imposes no limitations upon any process found by Congress to be necessary to sustain and regulate the commerce of the nation. If the shipper pays slightly more to one carrier than he would if the rate level were determined accordingly to that carrier's condition, that consequence is necessary in the regulation of commerce, and he pays slightly less to other railroads than the rate authorities might properly allow. He has no right to insist that the fate of the agencies of transportation shall hang on his

asserted right to isolate for inquiry at any moment the question of every rate for every single shipment over any particular carrier.

Again, the excess paid to the stronger carrier is so slight as to each shipment as to be negligible under the principle of *de minimis*. It becomes appreciable only when the total revenue of the carrier is computed. Clear violation of a constitution is never *de minimis* but the constitution deals with practical and tangible considerations and is not sensitive to microscopic complaints against legislation necessary to move the commerce of a nation.

We have already adverted to the fact that the shipper's right to pay each carrier only what is the minimum reasonable rate for each service by that carrier is not an individual right secured by the Constitution against modification. It is, on the contrary, a derivative common law right, *based on the public interest with which the business is affected*, and is subject to any legislation found necessary by Congress under the commerce clause; for Congress can change the common law relationship between shipper and carrier whenever necessary in the public interest in the regulation of commerce, just as it has changed the common law liability and relationship between the interstate carrier and its employees, between the carrier and shippers in respect to limitations of liability, as well as other vital common law relationships found inconsistent with the regulation of commerce. *In fact, any legislation regulating commerce changes the common law status unless merely declaratory.* *Wilson v. New*, 243 U. S.

332, 347. Finally, the excess earnings to be received by sundry carriers are to be recaptured and expended in a very substantial sense in the interest of the service of the shippers who have produced them, such as in the acquisition of reserve or floating equipment which will directly tend to avoid car shortage and reduce operating expenses and rates.

A strictly analogous provision of undoubted validity is found in the Commerce Act, asserting that rates must be reasonable and authorizing an individual shipper to sue for reparation and by this means recapture the unreasonable excess earning received by the carrier on specific shipments under a rate which was at the time of shipment the published prevailing rate. Prior to the amendment of 1906 this was the only recourse possessed by the shipper against the imposition of unreasonable rates, who was nevertheless compelled by law to pay the published rate, whether reasonable or unreasonable. The difference between the right of Congress to make the rate final and legal as to the shipper and yet hold the question open as to the Government is established. *Keogh v. C. & N. W.*, 260 U. S. 156.

The consolidations contemplated by the Transportation Act of roads of dense traffic with roads of lighter traffic are nothing but grouping made absolute. It would be fatuous to suggest that the shipper has a right to prevent such consolidations on the theory that by forcing the light-traffic roads to remain independent and accept rate levels adequate for the roads of dense traffic the shipper

could get lower rates ~~than may~~ be demanded by the consolidated property.

In the present case the recapture of the excess is by the Government in pursuance of the power of regulation. The excess earning is administered for the general use of the shipping public, which has produced the excess, and in order to avoid the destruction of competition.

Analogies to this intervention by the Government for the transfer and administration of funds which the holder has no constitutional right to retain are not necessary to the argument, but one may be found in the Massachusetts statute requiring savings banks to pay over unclaimed deposits to the State Treasurer for administration by him as trustee. This constitutes no taking from the savings bank. *Provident Inst. for Savings v. Malone*, 221 U. S. 660.

An interesting and just analogy is the credit allowed on premiums on mutual policies resulting from an arbitrary loading of the premium level to cover prospective and unascertainable extra risk and expense. This loading almost invariably proves excessive and the difference between the amount loaded and the amount which actually proved necessary is returned under the insurance term "dividend."

"This difference, however, is not in any real sense a dividend. * * * This excess payment represents, *not profits or receipts but an overpayment*—an overpayment because, being entitled to his insurance at cost and having paid more than it cost, he is equitably entitled to have such excess applied for his benefit."

Mutual Benefit Life Ins. Co. v. Herold, 196 Fed. 199.

Connecticut Gen. Life Ins. Co. v. Eaton, 218 Fed. 188; *id. v. id.*, 218 Fed. 206.

Penn Mutual Co. v. Lederer, 252 U. S. 523.

(It is plain that the carrier need not pay income taxes on that part of its excess earnings paid into the general railway contingent fund, if it makes a proper return.)

The difficulty in many cases of determining who should recover and hold the excess over a reasonable rate paid in ordinary cases has resulted in the affirmative provision of the present Commerce Act that the shipper shall recover it, although he may have passed on the loss to the consignee, and the latter may have passed it on to the general public. As said by Justice Holmes in speaking of the Commerce Act in *Southern Pac. R. Co. v. Darnell*, 245 U. S. 531, 534, "the carrier ought not to be allowed to retain his illegal profit, and the only one who can take it away from him is the one that alone was in relation with him and from whom the carrier took the sum." This by no means intends to suggest that Congress can not follow the inquiry further as to the final incidence of any such excess.

The right of reparation for specific overcharge is left undisturbed by the Transportation Act. It would be clearly within the power of Congress to restrict reparation to the consignee or whoever finally sustained the damage due to the overcharge. There is, of course, no reason why Congress should not now recognize the fact that the burden and final incidence of the excess earning (to be conditionally permitted in order to sustain competition in service and adequately to regulate

commerce) would fall upon the general public, made up of indistinguishable persons and inadmeasurable amounts, and should, therefore, be recovered and administered by Congress for the general benefit of the public interest in transportation.

INTRASTATE EARNINGS

This excess earnings reduction involves no unconstitutional recapture of the earnings resulting from intrastate operations. In ordinary cases only about 25 per cent of the traffic of the railroads is intrastate, and about 30 per cent of the revenue is derived from intrastate business. The ratio in this particular case is higher, but Congress is not required to abstain from a rule of regulation because its necessary generality will not affect all units exactly alike. See authorities, Proposition X, *supra*.

It is common knowledge that intrastate operations are normally more expensive and the proportion of net earnings less, so, as a clearly established general rule the net earnings of interstate carriers will rarely ever equal one-third of their total. As it is proposed to permit them to retain all of their net earnings up to 6 per cent and one-half of the excess, it is clear that as a general rule this *one-half* will give them more than their total net earnings (not already embraced in the original 6 per cent) from intrastate revenue. If extraordinary cases exist, in which this shall appear not to be true, the railroad has recourse to the Commission under the reasonable rules prescribed and to be prescribed by it pursuant to the Act or to the courts to permit it to show that it is entitled to

retain a greater percentage of its excess earnings over the standard of 6 per cent plus the stipulated division over that ratio—authorized by the Act.

The foregoing answers the "intrastate" objection on the narrow basis on which it is urged. There is a conclusive answer on much broader grounds. Under the Transportation Act, the relation between intrastate rates and interstate rates is expressly subjected to the jurisdiction of the Interstate Commerce Commission (*Wisconsin Passenger Fare Case*, 257 U. S. 563; *New York v. United States et al.*, 257 U. S. 591); and where necessary to maintain the proper relationship the Federal body is given direct control over individual intrastate rates.

The recapture provision of Section 15a is a further express exertion by Congress of its jurisdiction over the interstate carrier. It is manifestly impracticable to provide for a segregation of the value of the carrier property engaged in interstate commerce from that proportion engaged in intrastate as a matter of routine regulation, or for a like separation of operating expenses. *Congress had the discretion to refrain altogether from the regulatory mechanism established by Section 15a or to apply it to the excess revenues of interstate carriers from whatever carrier operations derived.* It followed the latter course.

Of the plenary authority of Congress under the commerce clause to occupy the entire field of regulation of interstate carriers or to stop short at any point in its discretion, there can be no doubt what-

ever; and there can be no doubt that it is the purpose and intent of Section 15a to occupy so much of the field as is necessary to apply the test of reasonableness to aggregate carrier revenue, allowing the diligent and favorably located carrier to retain one-half of such excess. The result to the Dayton-Goose Creek Company is to leave it with a return of from 8 per cent to 8.2 per cent on its own asserted value of its property. It is difficult to discern confiscation in that result.

It is, accordingly, apparent that what are objected to as novel features are mere details in the mechanism employed to work out an established principle. At the time of the decision of *Munn v. Illinois* and the *Granger Cases*, it was asserted that regulation of rates meant the destruction of efficiency and energy, just as the opponents of this measure before Congress asserted that the proposal "is fraught with consequences to our institutions and to our national safety too serious to be encountered." The argument now and the argument in those earlier days is the same, and both have been properly characterized by the Supreme Court:

"Against that conservatism of the mind which puts to question every new act of regulating legislation, and regards the legislation invalid or dangerous until it has become familiar, government—State and national—has pressed on in the general welfare."

RESERVE FUND PROVISIONS

We attach slight importance to the provision of the Act relating to the reserve fund to be built up

out of the moiety of excess earnings retained by the carrier. Those provisions (that is, as to the disposition of such moiety by the carrier) are not, in our opinion, essential to the fundamental requisite stated by sub-section 5. They appear to be indispensable neither to the theory or mechanism of successful regulation, and we are, frankly, unconcerned whether they are held to bear a fair relation to regulation of rates of interstate carriers or not. Our impression is that the reserve fund provision is separable and might well fail without bringing down the main provision and processes of the section. We say this without any suggestion whatever of doubt as to the entire validity of the reserve fund requirement, for we have none. It appears to be reasonably limited in amount. After that limit is attained all additional sums retained by the carrier may be employed for any proper corporate purpose without restriction. For these reasons we waste no time in response to the prolonged discussion of the reserve fund.

THE QUESTION OF THE TAXING POWER

Appellant assails that part of the opinion below which suggests arguendo that the excess earnings provision is in effect an excise tax. We do not consider that conclusion in any sense necessary to sustain the provision. Undoubtedly there is a sound analogy in the process to the familiar recapture of benefits gratuitously conferred under the name of taxation. In this case the benefit conferred is the excess revenue over a reasonable return tentatively and conditionally permitted to the carrier. Such benefits are notoriously subject to

recapture by the state. We refer to this process in Propositions X and XII *infra* and have no doubt whatever of the correctness of the analogy. To that extent the Special Court was quite warranted in referring to the process as a species of tax; but that nomenclature is plainly unnecessary to sustain the legislation. It is, primarily and directly *regulation* and needs no other alibi. The mechanism employed has many sound analogies—but it is, after all, *regulation* under the Commerce Clause. The fact that the recapture of a gratuity is not violative of the Fifth Amendment is the important fact.

THE PRINCIPAL GROUNDS OF OPPOSITION TO THE
THEORY OF SECTION 15(a)

It has seemed certain to the association of security owners that the theory of section 15(a) is integral; that there is no hope for obtaining the salutary provision of paragraphs (2), (3) and (4) of the section or preserving those sections in the law without the provisions for the regulation of excess earnings which would inevitably be produced if the rate level produced under those paragraphs is pitched at a point which will sustain transportation as a whole.

It may be that this Court would hold that paragraphs (2), (3) and 4 might stand even if the remainder of the section for the regulation of excess earnings were declared invalid. We doubt that result as a matter of law. We are fully assured that as a matter of legislative expediency the hope to sustain paragraphs (2), (3) and 4

would be vain if the remainder of the section were declared unenforceable.

For this reason the association of security owners is profoundly concerned at the disposition of a limited number of the railroads to contest the sound integral theory of section 15(a). The section brings forward into rate making those essential revenue considerations which undoubtedly protected a large number of the American railroads from certain disaster as the railroads emerged from Federal control, through disintegration of their rates. It is today the one assurance that rate making—by state and by nation—will proceed on a rational and constructive basis.

We therefore consider that the position taken by the general counsel for the opposing lines is not only unsound in point of law, but in point of economics and legislative expediency when they urge that the rate making provisions be let alone and the remainder of the section be annulled (Brief of Messrs. J. P. Blair and others, p. 7).

They assert that paragraphs (2), (3) and (4) properly regulate rates—although its basic consideration is *revenue* and *return*, but assert that the provisions which they oppose are not a regulation of rates; that they merely take income not in and of itself a part of interstate commerce (*id.*, p. 8, *et seq.*). In short, paragraphs (2), (3) and (4) dealing with “fair return” is a regulation of rates, but paragraphs (5) *et seq.*, also dealing with “fair return” is not a regulation of rates.

Their suggestion mutilates the synthesis of section 15(a), which makes it plain that the

higher level of rates encouraged by section 15(a) in order to assure a fair return to the average carrier is primarily and from the outset conditioned upon the concurrent proposal for the regulation of the resulting excess over fair return to particular carriers which is being intentionally produced. The purpose to regulate the excess is, accordingly, from the outset an inherent part of the process of establishing the rate structure itself.

Of like nature is the suggestion (*id.*, p. 19) that rates are presumed to be reasonable and that a carrier has no right to "retain collections of transportation charges which are unreasonable." The fallacy of this suggestion has been fully discussed. It has been demonstrated that rates may be made final as to the individual shipper, in order to sustain transportation as a whole, but left as an open question to the government applying its regulations in the interest of transportation.

The chief point of attack on the process is based on the theory that those carriers for which excess earnings will be produced by the competitive level necessary to sustain the average carrier have a constitutional right to have this competitive advantage reflected in excess revenue (*id.* p. 24-41, etc). That is a conclusion which cannot be conceded. It is vigorously pressed not only as a basis for the argument that their revenue derived from competitive rates thus conditionally permitted, shall not be subjected to the test of reasonableness, but as a predicate for consideration in connection with valuation. It is insisted that this relative superiority of advantage is a property right which is

immune from regulation in terms of rates or revenue. Their superiority of location and circumstance is not "taken." Their real objection is that it may not be limited in terms of return under the Commerce Clause by any process which will adapt the rate structure to the status of a fair return on their properties, unless a like process is applied to their competitors—so that the *relative* earning power will be maintained. In short, they assert that their rates (and consequently their revenue) can be regulated only by making rates which are final and unconditional for all purposes—both for themselves and their competitors.

If they are correct that insistence brings about a portentous situation in transportation in America. It means that a large part of our systems will be forced out of business or to indefinite reorganizations each decade; for it is certain that a dollar invested in a line of secondary earning power is in close competition with a line of greater earning capacity can never hope to attain a fair and reasonable return on the new investment constantly required, on rates averaged down by the lower operating costs of the competitor.

This conclusion is inevitable because of an intensely practical consideration. It is obvious that neither Congress, the Commission nor the public will in the future—as they have not in the past—be willing to create rate structures which will produce what will be considered excessive returns for the more advantageously located railroad. So the position asserted by the opponents of this process is, in effect, a sentence of disaster.

This attitude of the opposition is not left in doubt. They insist that this "differential" in earning power, translated into revenue, is a property right which may neither be taken or regulated—although the owner is left with a reasonable return upon the full fair value of the property—all elements of value considered. That is a solecism on its face.

It is obvious that they are demanding—not the protection of value, but *value in relation to their competitors*—which is a very different thing. They might with much reason insist upon a constitutional or property right to exact a lower rate than their competitors because of the less cost of transportation over their lines. But they are willing to waive this right and charge a rate which is, as to them and in and of itself, unreasonable, provided it is made unconditional and they can retain all of it.

In short, they assent in effect that the process would be all right if there were only one railroad. It would be regulation that would not impair *relative* advantages, but it must not be permitted as to group competitive railroads.

We see no justification in that position. It threads opponents arguments (id. 25-28, etc).

A further thought that opponents advance is that the trust clause (paragraph (5)) is not competent to relate back to the rates themselves and is therefore inoperative and leaves the process essentially *ex post facto* in character. (id. 28, *et seq.*). That is a pretty narrow suggestion. We consider it unsound in fact; and irrelevant. The

essential fact is that Congress has in advance admonished the carrier of the process and that the revenue is received subject to the statutory mechanism. There is no constitutional reason why Congress could not refrain from regulating rates at all, leaving their excessive results to be regulated by recapture, under statute existing when collected, for administration in the interest of the shipping public which produced the excess.

Opponents attack the theory of classification (*id.*, p. 41, *et seq.*). We have fully discussed that subject (Proposition XV, *ante*) making plain that the regulatory agency may adapt the rate structure to the circumstances of the different carriers. This established process is plainly what is accomplished in a rational way by section 15a. That long established process, moreover, effectually disposes of the assertion of a property right, immune from regulation, to charge the same or a lower rate than a competitor; in short the revenue differential for which opponents contend.

The substance of the attack on this process is that such adjustment of the rate structure to the circumstances of different carriers is not practicable by the old methods because the carriers involved are in competition and the rates must actually be the same unless the carrier having higher cost of operation is to be dried up (*id.* 45-6). Section 15a has found the method of arriving at the objective without the adverse result; and counsels' quarrel is necessarily with the success rather than the validity of the process. Such objection in detail as is defined is that the recap-

ture has no rational relation to the rate and is not therefore "rate regulation." (id. 47.) We have seen that the Commerce Clause is not restricted to rate regulation in the common law sense—but covers regulation in all appropriate phases necessary to conserve commerce as a whole which leaves the particular carrier with a reasonable return upon the fair value of its property or a fair opportunity to earn it. But we do not agree at all with counsels' suggestion that it is not rate regulation.

NEW ENGLAND DIVISIONS CASE

Counsel's distinction of this case from certain comments in the *New England Divisions Case* (id. p. 51) is predicated upon an attempt to distinguish the bearing of public policy made effective in that case as applied to divisions of rates from the bearing of public policy made effective by 15a as to the revenue conditionally derived from rates. While the case cited is not decisive in fact of the question at bar the distinction attempted is not sound. It confuses principle with mere mechanism and amounts to no more than the contention that it is arbitrary and irrational to deal with rates through making them tentative as to their aggregate result and dealing with the result. We have fully discussed the rational process of regulation through dealing with results rather than with the guess basis of fixing individual rates. The effect of the rate making provisions in their entire operation is to apply both tests. They are tentatively made on the best basis practicable and checked by the actual test of results.

We do agree that the observation in the *New*

England Divisions Case, p. 191, suggesting that section 15a aids weak roads directly through the recapture from prosperous competitors of surplus revenue, is inadvertent, ~~is~~ ^{as} contended by counsel for the opposing railroads (*id.* p. 51). The direct advantage to the roads of relatively low earning power lies in the fact that section 15a makes possible a higher rate level through the assurance to the public and to the regulating agencies that exorbitant surpluses produced by such rate level in particular cases will be regulated.

In opening their second point, counsel for the opposition assert that the excess-earnings clause is not a rational regulation of rates for the reason that "the amount of net income is arbitrarily made the sole and conclusive measure of the unreasonableness of rates" (*id.* p. 52 et seq.) That objection is certainly untenable. Assuming the good faith of the carrier in its efforts in the direction of efficiency and in keeping its accounts, what test could be more rational and fairer than the test of actual results? We have shown that the courts frequently require an actual test before entertaining a suit to restrain rates. On what basis can it be suggested that Congress may not employ the absolute test of actual results?

Counsel assert (*id.* p. 54-59) that the test of net return is not an absolute measure for individual rates—that even if the return is reasonable, arbitrary action (such as the Dakota coal rate law—*Northern Pacific v. North Dakota*, 236 U. S. 585) will not be sustained. There is nothing in section 15a to interfere with this doctrine; but as we are

now dealing with rates in the aggregate it can not be asserted that a process which leaves a fair return is arbitrary. It is moreover too late to suggest that carriers have a constitutional right to insist upon rates in the aggregate which will produce more than a reasonable return and section 15(a) throughout deals with revenue or return in the aggregate. See Proposition XII, *supra*.

They also cite (id. p. 59) the Cotting Case in which a dictum of Justice Brewer (six of the Justices not concurring) exalted the reasonableness of the charge for each unit of service as the test, in and of itself, of reasonableness without reference to the aggregate result. A sufficient answer to the citation is that the unit test has long since been found unworkable. Were it otherwise, the common law, unaided by commission, state or national, would have sufficiently regulated rates. When each jury arrived at a different result, it was seen that this process was useless as a uniform or definite test; that a single conclusion (that of a commission) must be substituted for the diverse conclusions of many. This means, of course, that the reasonableness of any given rate is at best a guess. We must still employ that process in dealing with individual rates; but when we are dealing with rates in the aggregate—with the revenue considerations necessary to sustain the agencies of transportation it would be irrational, even fatuous, to employ the inch measure of individual rates. That is counsels' continuing and egregious error. They decline to deal with rates in the aggregate although that is exactly what section

15a deals with—paragraphs (2), (3) and (4) as well as (5) and (6). They are apparently willing to deal with rates in the aggregate in getting the rate level tentatively established but are unwilling to continue the process to the logical result worked out in paragraphs (5) and (6).

For a generation counsel for the railroads proceeded with their unit or inch measure theory and brought the railroads to the brink of disaster. Thoroughly alarmed, the main body of security holders urged Congress to adopt a revenue test and to extend responsibility for applying it to the Commission. The net effect of counsels' argument is to force rate making and rate adjustments away from revenue considerations as the underlying test to the outworn and impracticable process which came near destroying these properties.

It is several generations too late to complain of testing the reasonableness of rates as a whole by testing the result (Proposition XIII, *supra*). We therefore attach no importance to the dictum in the *Cotting Case* or the other authorities to the same effect cited by counsel (8 App. Cas. 723, etc.). Equally unjustified is the contention that the test of actual results is so arbitrary as to amount to a denial of due process (*id.* p. 66). We confess that we can not regard as seriously intended any such assertion.

Counsel asserts that rates cannot be increased, if reasonable in and of themselves, merely because they are not compensatory (*id.* 68). That suggestion begs the question—and drops back to the consideration of individual rates, a subject with

which section 15a does not deal. It is, moreover, misleading. We have shown that reasonable rates from the public standpoint are generally speaking those rates which the public would have to pay to reproduce the same services (*Brunswick, etc. District v. Maine Water Co., supra*)—bearing in mind here, of course, that section 15a is dealing with the service rendered by a national system of transportation conducted by competitive units. Rates would certainly be unreasonable to the carriers which failed to enable the agencies themselves to survive—under honest and efficient management; and section 15a asserts that proposition as the statutory policy of the United States.

One of the stubbornly asserted criticisms of the opponents of this process is that “if rates are unreasonable they have always been recoverable” and that “they are, and always have been, unlawful exactions in so far as they exceed what is reasonable” (*id.* p. 53). That observation is neither logical nor correct in that it confuses the two applications of the term “reasonable” as applied to the making of rates for competitive systems under a national scheme. We have elsewhere pointed out that it may be reasonable for the shipper to pay a uniform rate in order to sustain competitive service that may yet be actually unreasonable for particular carriers in the group to receive. It is, as we have shown, clearly reasonable for the shipper to pay that which is necessary to sustain the competitive agencies of transportation even if it is *loaded* as proposed by section 15a to accomplish that result. But that is very dif-

ferent from the question as to what is reasonable for the carrier to receive for the service. Since a rate may be closed as to the shipper and left open as to the government (*Keogh v. C. & N. W.*, *supra*), it is entirely proper that the latter process should be employed to avoid either of the consequences which would follow if its opponents should prevail. Either the public by patronizing the competitor with the lower rate structure would dry up its parallel or competing line, or excessive revenue would be permitted to the lines with denser traffic. The latter result would be a constant impediment to fair rate structures.

A number of cases are cited (*id.* 70-74, 80-82) by opponents in support of the well settled proposition that in establishing competitive rates the rate making authority is accustomed to give consideration to the entire competitive situation and does not base the rate necessarily on the line having the shortest haul or most favorable operating conditions or densest traffic. That is good public policy—necessary to sustain competitive line. Obviously the shipper can not complain. We have shown that his rights are not primary but derivative, as a member of the general public. (Propositions XVIII and XI.) That rate making policy ~~that~~ is very different from a contention advanced by the line of shortest route, or lowest operating cost or densest traffic, that is *has a constitutional right* to have a rate made on a competitive or group basis rather than on another basis justified by the cost of the service to it.

As for the contention that the question of “rea-

sonable rates" must depend primarily upon the reasonableness to the shipper of each rate for the individual service involved (*id.* 67, 74), it is clear that we are tendered a standard which is wholly impracticable of application or assistance in the adjustment of general rate levels for a national railway system. More and more steadily has the rate making authority passed from the effort to analyze each rate in and of itself. An examination of the reports of the Interstate Commerce Commission discloses that the question of rate making, in detail as in the adjustment of the general rate level to changes in the cost of transportation has resolved itself into a process of relations, comparisons and adjustments of inequalities, checked finally and in the aggregate by net railway operating income.

We have several times referred to the sound doctrine stated in *Brunswick, etc. Dist. v. Maine Water Co.*, that in general and subject to the proposition that the public should pay something for the risk of capital which it avoids, a reasonable charge for any given public service is that which it would cost the public itself to reproduce the service. In this case the service is the actual service performed *plus a stand-by service* rendered by the competitor. It is inequitable for the carrier rendering the service to retain the stand-by charge where the total is in excess of the cost and a reasonable profit to that particular carrier; stated otherwise, a shipper has available two or more routes, uses only one, and pays for the privilege. That is inherent in the public policy of inviting

and sustaining a great national system made up of competitive units.

Opponents persistently decline to recognize this distinction between a rate which may be reasonable for the shipper to pay and one which may be reasonable for the carrier to retain (*id.*, 79-80.) The assertion is made by counsel (*id.*, 85, *et seq.*) that the right of the government to regulate the charges for the use of properties impressed with a public trust rests upon the theory that without such regulation the owner may exact from individual patrons unreasonably high rates. That may be truly stated as an expression of the common law right which passed to the states, but it is not a correct statement of the power of Congress under the Commerce Clause, which was plenary in the sense that Congress was authorized to make such regulations as are necessary to preserve and protect interstate commerce and its agencies on a wholesome basis, and all interstate carrier properties are acquired subject to that condition. That power is clearly broader than the mere rate making power inherent in local authority. It is quite conceivable, under the theory for which the opponents of this statute contend (that is, that Congress may not regulate differential advantages inherent in location, or in low cost of construction or of operation or density of traffic) that railroads exceptionally located might become a menace, by virtue of their exceptional situation, to the existence of all other essential agencies of transportation. We do not find it necessary to take the position that such predominating influence might

invest such carrier with noxious consequences in the sense that it might be considered in the class of hurtful agencies which may be excluded from commerce altogether, but it is not to be doubted that the power of Congress under the Commerce Clause on such a premise is broader than mere authority to try and ascertain whether or not the rates and fares charged to the public by this agency were exorbitant. We believe that the Commerce Clause can reach the carrier itself whose assertion of competitive advantage endows it with qualities which menace the agencies of transportation as a whole.

We note again the persistent refusal of the opponents of this process (*id.*, p. 89 *et seq.*) to distinguish between the establishment of individual rates which are just and reasonable in relation to other rates and are proper for the shipper to pay—especially to sustain the competitive agencies of transportation—and the conditions which Congress may attach to the receipt of those rates by carriers for whom they produce an excessive return. Having repeatedly conceded (*id.*, p. 89, *etc.*) that paragraphs (2), (3) and (4) constitute proper regulation of commerce and that one of the objectives was to get a rate level “*which would produce revenue adequate to sustain the average roads and probably better the former condition of the weak roads of the group,*” counsel illogically assert that ~~the objection of~~ paragraphs (5) and (6) had as their object a third and entirely distinct object: “namely, to prevent the better-than-average carrier of a group from retaining

net income realized from the rates prescribed under the new rule of rate making in excess of the rate of return fixed by the Act" and that this third object cannot be said to be accomplished by a regulation of commerce in that the net income arises after the act of commerce has been completed. To reach this narrow and tenuous conclusion counsel deny the validity of the integral nature of the process proclaimed in terms by the statute (*id.*, p. 89, 90).

In conclusion, we restate our belief that the rejection of the provisions of section 15a now under attack would make imminent or assured the restoration of the old, unsatisfactory and destructive basis of rate making, withdraw the provisions placing transportation on a truly national basis, and destroy the revenue considerations which have protected these systems and now protect them from serious consequences.

Respectfully submitted,

JOHN G. MILBURN,
FORNEY JOHNSTON,

Of Counsel.

November, 1923.



APPENDIX

As part of the literature dealing with the theory and constitutionality of Section 15a are to be noted the recent article by Charles W. Bunn, Esq., entitled "The Recapitulation of Earnings Provisions of the Transportation Act," Yale Law Journal, January, 1923; the article by the writer of this brief entitled "The Transportation Act, 1920," in the Virginia Law Review, April, 1920; also his testimony before the Senate Committee on Interstate Commerce, November 23, 1921, in the hearings on S. 1150 and S. 2510 (Modification of Transportation Act, 1920), p. 475 et seq.

Among the notable expressions of able lawyers at the time of final consideration of the legislation before Congress are to be mentioned the following, sufficiently indicating the fundamental necessity for this legislation and the soundness of its economic and constitutional theory.

EXCERPT FROM SPECIAL ARTICLE ON TRANSPORTATION ACT (SENATE BILL), BY HON. WM. H. TAFT, THE PUBLIC LEDGER, PHILADELPHIA, PA., JANUARY 15, 1920.

"The problem which Senator Cummins has sought to solve is how uniform and reasonable rates may be fixed for the various railroads of the country so as to enable all of them to live and to prevent any of them from enjoying excessive dividends. To fix rates so low as directly to keep the dividends of certain railroads within reason would create impossible deficits for others in competition. The weaker railroads are necessary to the regions which they serve and must be maintained. If private operation is to continue, how can the matter be adjusted? Senator Cummins' method is to divide the country into rate districts in which conditions are similar, to ascertain the value of all the railroads within the district and then to fix rates at such a level that the net return for the use of the properties shall be $5\frac{1}{2}$ per cent on their value, with half a per cent more to be used by the railroads in nondividend-producing improvements. Any railroad earning more than

this is to divide the surplus, up to 7 per cent, equally with the Government; its half a per cent to be put in a reserve fund and the Government's half a per cent to be used to create a railway contingent fund. Should the revenue of any railroad exceed 7 per cent, one-fourth of that excess is to go into the Railway Reserve Fund and three-fourths into a Government Railway Contingent Fund. After the reserve fund of the railroad shall have reached and is maintained at 5 per cent of the value of its capital, the division of the excess over 6 per cent between the railroad and the Government is one-third to the railroad for such uses as it chooses and two-thirds to the Government Railway Contingent Fund.

* * *

"The merits of the Senate bill are that it furnishes a reasonable standard for the action of the Interstate Commerce Commission in fixing rates. It requires primarily the fixing of rates enabling the railway companies of the country to live and to pay a reasonable income on their property. With that as a fundamental rule, the rest of the problem will work itself out, because the change will restore confidence in railway properties as an investment. The deplorable phase of the present situation has been the impossibility of securing capital to make needed new construction.

"The 5½ per cent standard of rates has been called a guaranty, and has attracted criticism and objection. Shippers and certain groups of the interested public are not content to give up their fancied advantage in the present unsatisfactory system by which railroads are made to work for insufficient pay. Such a result in the end works against the shipper, because it reduces the possibility of adequate facilities and injures the whole railway service. But he cannot be made to see this. Five and one-half per cent on a value fixed by the Commission itself, after the fullest investigations, is not an excessive rate.

"On the other hand, objection comes from the successful railroad companies that this is not enough for them. They object that it is confis-

cation to take away from them an excess over 6 per cent and compel them to divide that excess with the Government, and, therefore, it is unconstitutional. The police power which may be exercised in the regulation of the rates charged by the railroads is ample for the purpose. It is not limited to any particular method by which those rates and the revenues from them shall be kept within reason. Rates may be fixed directly or they may be fixed with reference to the dividends which they bring, so that when the railroad actually receives its net revenue it becomes a trustee of the receipts until the fair return may be determined. It is only rate fixing after all."

EXCERPT FROM PAPER BY WALKER D. HINES, ESQ., DIRECTOR GENERAL OF RAILROADS, BEFORE ASSOCIATION OF THE BAR OF NEW YORK, JANUARY 7, 1920.

"First, I believe that there will not be a prompt and liberal treatment of rate questions until profits clearly in excess of a fair return are appropriated in part to the public interest.

"As an illustration, I have in mind one important railroad company whose railroad, even in this difficult year, will earn over 140 per cent of the standard return, and this company has in the past paid high dividends and in addition has had a large annual surplus. When the railroad companies apply for an increase in rates it will inevitably be urged that an increase ought not to be granted which would still further increase the large profits of this company. For example, an increase of 20 per cent in the freight rates of this company would give it a net operating income more than twice the standard return assuming that it continued to enjoy the same business. I have no doubt that such a prospect would stimulate the most persistent opposition to the increase and the result might be that an increase seriously needed by other companies would be defeated simply because the giving of the increase would yield what would be regarded as a grossly excessive profit for this favored company. I see no way to meet such a situation except to provide for a

division of the excess over a clearly reasonable return. Of course, enough of the excess should be given to the company to stimulate efficiency in operation, but beyond that point the fact that the company would get the excess would be a serious obstruction to the railroads in general getting an increase to which on the average they might be entitled. The excess thus appropriated for the public interest should be largely placed in reserves so as to protect the general railroad situation in unfavorable years. Such a course would quiet agitation, would stabilize the situation, and without it I believe it would be impossible to get prompt and liberal treatment of any rate increase question."

EXCERPT FROM PAPER BY HON. C. A. PROUTY, DIRECTOR,
BUREAU OF VALUATION, INTERSTATE COMMERCE COM-
MISSION, BOSTON, MASS., FEBRUARY 2, 1920.

"As I see it, it is this uncertainty more than everything else which has demoralized railroad credit, and if that is right such credit can only be restored by removing the uncertainty. In some way the Government must determine, first, the value of the property of each carrier upon which a fair return shall be allowed and, second, that rate of return.

* * * * *

"Having clearly stated the amount of return to which these carriers are entitled, the next thing is to devise a way in which such rates can be established as will yield that return and no more. This plainly must be by instructing the Interstate Commerce Commission to establish proper rates for that purpose and give the Commission the necessary authority to do so.

"The difficulty of this problem is comprehended in the three words above underscored, and no more. The rate must yield the carrier enough or it cannot function; it must not yield too much or the public is unjustly burdened. If the Interstate Commerce Commission were given, as it should be, the fullest authority over the making of rates and divisions, it would still find itself beset with certain practical difficul-

ties as to which it must have the aid of legislative enactment. These difficulties would be of two general classes, arising, first, from the competitive situation, and, second, from the fact that net earnings cannot be accurately forecast and must vary from year to year.

"The railroads of this country in a given section are generally competitive; that is, they must charge the same rate. But the application of that rate upon all the railroads in the competitive territory produces widely divergent results. Road AB earns a return of 20 per cent upon its value, and road XY only 3 per cent.

* * * * *

"The owners of this railroad have devoted its property to the public service. They are entitled to a fair return upon the value of that property and no more. Twenty per cent is manifestly an utterly extravagant return. This road has no vested right to prey upon the community which it serves. It is the duty of the Government, not to single out that particular road and appropriate its property, but to provide by general enactment that the net earnings of no railroad shall exceed what is reasonable. It may do this by fixing the rates which the road may charge, or by fixing the net income which it may earn, or by combining the two processes. The provisions of the Cummins Bill would allow this railroad an earning of between 9 and 10 per cent upon its value, which certainly is most munificent to those stockholders and not un-American unless it be un-American to restrain the rapacity of wealth.

"What shall be done with the surplus seems to me immaterial. It should be covered into the United States Treasury and appropriated for any proper purpose. What shall be done for the weak road, I am not now considering. That road under the proposed legislation would be vastly better off in the future than it has been in the past, although it will probably require additional assistance.

"The second embarrassment under which the Commission would act arises out of the fact that it is impossible to accurately forecast the

net earnings which will be produced from year to year under any given scale of rates.

* * * * *

"It has always seemed to me that if in any year the earnings of a particular carrier exceeded the amount to which it was entitled under the declaration of Congress, then the surplus should be put into a fund to be held for the payment of future interest and dividends in those years when its earnings did not equal the amount prescribed.

* * * * *

"The foregoing principles are embodied in the Cummins Bill. For many years I have been an advocate of these ideas and it is extremely gratifying that they have at last found favor with the Senate committee which has given this whole subject the most painstaking and intelligent consideration. Personally, I believe that Section 6 is more important than any other item in the pending legislation, for I do not believe that private operation can be permanently successful without some plan of this sort."

EXCESS EARNINGS OF RAILROADS

LETTER FROM
THE CHAIRMAN OF THE INTERSTATE
COMMERCE COMMISSION

TRANSMITTING

IN RESPONSE TO A SENATE RESOLUTION OF
DECEMBER 15, 1922, INFORMATION RELATIVE
TO THE DETERMINATION AND RECOVERY OF
EXCESS RAILWAY OPERATING INCOME



DECEMBER 27 (calendar day, DECEMBER 30), 1922.—Referred
to the Committee on Interstate Commerce

WASHINGTON
GOVERNMENT PRINTING OFFICE
1923

tion 19a of the act. Such valuations, however, date back from four to eight years and have not as yet been brought up to the periods affected by the statute. This will involve considerable accounting and engineering work in connection with the checking up of additions and retirements.

The limited appropriations for the valuation of carriers have during the last two years forced us to choose between the curtailment of our activities in fixing and issuing tentative valuations as of specific dates of valuation or deferring the work of bringing valuations up to date. We adopted the latter alternative. The bringing of valuations up to date is, however, receiving active attention. We now have men in the field and in the Washington office engaged in bringing up to date the valuations of some 40 carriers whose returns indicate that their earnings may be subject to the recapture provisions of section 15a. Due to lack of sufficient appropriation in the present fiscal year, this work is limited to the class of carriers named. Progress in this vital work in the fiscal year 1923-24 is contingent upon the appropriation which may be granted by Congress for valuation work. The estimate of \$1,000,000 recommended by the Bureau of the Budget does not include any allowance for bringing valuations up to date or investigations for the ascertainment of basic values for recapture purposes. Our representatives have explained to the House Committee on Appropriation the need of restoring our original estimate of \$1,280,000, which includes \$180,000 for policing returns made by carriers to our Valuation Order No. 3, dealing with additions, betterments, and retirements since the initial date of valuation fixed separately for each carrier, and for utilizing these returns in bringing valuations up to date.

Information concerning those railroads whose properties we have tentatively valued is contained in Exhibit B. The value of railway property as ascertained by the commission stated in this exhibit is in each case the tentative value as of the date shown, ascertained under section 19a.

No class 1 railroad has paid any excess earnings to the commission. Three class 1 railroads reported excess earnings, namely:

The Buffalo & Susquehanna Corporation, the Detroit & Toledo Shore Line, the Lehigh & New England Railroad Co.

These roads are included in Exhibit B.

(3) All other Class I railroads which, from any reports made to the commission, annual, monthly, or otherwise, appear to have received in excess of 6 per cent upon the value of their railway property; the value of such property of each found or approximately determined as aforesaid; and the excess earnings of each computed according to such value, or the nearest approximate estimate of the same which can be readily reported.

All Class I carriers have been included under paragraph (2), and there is therefore nothing additional to report under this paragraph.

(4) Each railroad other than a Class I railroad that has reported any excess earnings to the commission under section 15a; the value of the railway property of each, as claimed by it; the excess earnings admitted by it; the value of the railway property of each such railroad as found or determined by the commission as aforesaid; the excess earnings of each such railroad as computed on such value so found or determined by the commission; and the amount of excess earnings paid by each such railroad to the commission.

Twenty-six other than Class I railroads reported excess earnings, and are listed in Exhibit C. What has been said in paragraph (2)

relative to the ascertainment of the value of railway property is applicable here also.

(5) The aggregate of excess earnings which remain payable to the commission from all railroads, according to the provisions of said section 15a, as computed by the commission, or the nearest approximation or estimate thereof, which the commission can readily report; and the items which make up the aggregate to the extent that the same have been separately computed or estimated.

No information is available other than that shown in Exhibits B and C.

(6) Whether any railroad which has failed or refused to make any report as to excess earnings required by such rules and regulations as the commission may have prescribed, or to pay over one-half of such excess earnings in accordance with the provisions of said section 15a, has made any statement of its grounds or reasons for such failure or refusal; and, if so, the name of each such railroad with a copy of such portion of such statement as sets out such grounds or reasons.

All Class I railroads have made reports in response to our orders as to their excess earnings, although many have done so under protest. While the matter of furnishing reports is still the subject of correspondence with a few other than Class I carriers, no carrier has refused to make such report. In Exhibit D, attached hereto, the name of each railroad which has failed or refused to pay to the United States one-half of the excess earnings reported by it is shown, and the grounds or reasons given by each for such failure or refusal are stated.

(7) As to any railroad or railroads appearing to have received in trust for the United States excess earnings which remain payable to the commission, according to the provisions of said section 15a, the steps or proceedings taken or begun by the commission to enforce payment of the public moneys so unlawfully retained.

The provisions of the law bearing upon the enforcement of section 15a and the orders of the commission thereunder have been carefully studied by our legal advisers with a view to the institution of proper legal proceedings against delinquent carriers. A number of cases have been examined in this connection but no suits have been instituted by us.

The Dayton-Goose Creek Railway Co., by bill filed in the District Court of the United States for the Eastern District of Texas, on December 6, 1922, in Dayton-Goose Creek Railway Co. v. The United States of America et al., Equity No. 262, has applied for an injunction to restrain the enforcement of our orders referred to in paragraph (1) of this report, as directed against that carrier. This application is set for hearing at New Orleans, La., on Thursday, January 25, 1923, at 10 o'clock a. m. It is understood that the principal purpose of this proceeding is to test the constitutionality of the so-called recapitulation provisions of section 15a of the act.

(8) That the commission report the amount of the value of each of the railroads in each State, respectively, so far as the same has been compiled.

Up to the present time we have not undertaken to segregate by States the single sum value of interstate carriers. We have listed and shown separately by States in the tentative valuation reports thus far served the property of carriers with a fixed situs therein together with the cost of reproduction new and cost of reproduction less depreciation, except in the case of lands where present value is shown. We have not, however, allocated to States the general items of equipment, materials and supplies, working capital, or other elements of

value without a fixed situs in any one State. In assembling data upon which the value of a given carrier as a whole is based, we have collected the basic material from which information as to the values separately by States can be compiled. This is an activity for which no allowance is made in our valuation appropriation recommended by the Bureau of Budget for the next fiscal year and transmitted to Congress. The recommended appropriation, we specifically understand, does not provide for any undeveloped work. Except, therefore, for the inventories and elements of value above enumerated the information called for is not at this time available.

C. C. McCHORD, *Chairman.*

EXHIBIT A.

[Interstate Commerce Commission, Washington.]

ORDER.

At a session of the Interstate Commerce Commission, Division 4, held at its office in Washington, D. C., on the 16th day of January, A. D. 1922. In the matter of the recovery and payment of excess railway operating income under the provisions of section 15a of the interstate commerce act.

The commission having under consideration the provisions of paragraphs (6) and (9) of section 15a of the interstate commerce act, reading as follows:

"(6) If, under the provisions of this section, any carrier receives for any year a net railway operating income in excess of 6 per centum of the value of the railway property held for and used by it in the service of transportation, one-half of such excess shall be placed in a reserve fund established and maintained by such carrier, and the remaining one-half thereof shall, within the first four months following the close of the period for which such computation is made, be recoverable by and paid to the commission for the purpose of establishing and maintaining a general railroad contingent fund as hereinafter described. For the purposes of this paragraph the value of the railway property and the net railway operating income of a group of carriers, which the commission finds are under common control and management and are operated as a single system, shall be computed for the system as a whole irrespective of the separate ownership and accounting returns of the various parts of such system. In the case of any carrier which has accepted the provisions of section 209 of this amendatory act the provisions of this paragraph shall not be applicable to the income for any period prior to September 1, 1920. The value of such railway property shall be determined by the commission in the manner provided in paragraph (4).

"(9) The commission shall prescribe rules and regulations for the determination and recovery of the excess income payable to it under this section, and may require such security and prescribe such reasonable terms and conditions in connection therewith as it may find necessary. The commission shall make proper adjustments to provide for the computation of excess income for a portion of the year, and for a year in which a change in the percentage constituting a fair return or in the value of a carrier's railway property becomes effective."

It is ordered:

1. That the years or parts of years for which net railway operating income and the return represented by such income upon the aggregate value of railway property held for and used in the service of transportation are to be computed shall be the years or parts of years ending on December 31, respectively. In the case of any carrier which accepted the provisions of section 209 of the transportation act, 1920, the first period for which such computations are to be made shall be September 1, 1920, to December 31, 1920, both inclusive. In the case of carriers which did not accept the provisions of said section 209 of the transportation act, 1920, the first period for which such computations are to be made shall be March 1 1920, to December 31, 1920, both inclusive.

2. That the excess income for the portions of a year ended December 31, 1920, shall be preliminarily fixed as the income in excess of such proportions of 6 per cent on the value of the railway property held for and used in the service of transportation

as the net railway operating income for the months of September to December, both inclusive, or for the months of March to December, both inclusive, as the case may be, in the three years ended June 30, 1917, bears to the total net railway operating income for the same three years.

3. The aggregate value of the railway property of the reporting carrier or carriers held for and used in the service of transportation shall be based preliminarily, in the case of carriers which made such returns directly or indirectly, upon the amount reported or used by such carrier or carriers as the aggregate value of railway property held for and used by them in the service of transportation in the proceeding entitled "in the matter of the applications of carriers in official, southern, and western classification territories for authority to increase rates," Docket No. Ex Parte 74, with adjustments for—

- (a) New lines, extensions and additions, and betterments;
- (b) Retirements;
- (c) Amounts of property for which permission to retain earnings under paragraph (b) of section 15a of the interstate commerce act has been granted; and
- (d) Other increases or decreases,

properly affecting the aggregate value of the railway property of such carriers held for and used in the service of transportation, claimed or reported by the carrier and supported by detailed explanations. The value of such railway property, as reported, will be corrected, and the actual value will be determined in the manner provided in paragraph (4) of section 15a of the interstate commerce act, and corresponding adjustments in amounts recoverable by and payable to the commission will be effected. In the case of those carriers which did not directly or indirectly make returns in connection with Ex Parte 74, the investment in road and equipment as of December 31, 1919, with proper adjustments as hereinabove indicated will be used for preliminary computations, and these preliminary computations will be similarly corrected after the determination of actual values in accordance with paragraph (4) of section 15a of the interstate commerce act.

4. The establishment of preliminary bases for prorating the return of 6 per cent, or ascertaining property values to which the rate is applicable, does not preclude any carrier from using such other bases as it considers more equitable and in accord with the facts; such other bases, however, must be fully and properly supported.

It is further ordered, That pursuant to the foregoing rules and regulations for the determination and recovery of the excess income payable under section 15a of the interstate commerce act each and every carrier by railroad, or partly by railroad and partly by water, within the continental United States, subject to the provisions of the interstate commerce act, excluding—

- (a) Sleeping-car companies and express companies;
- (b) Street or suburban electric railways unless operated as a part of a general steam railroad system of transportation;
- (c) Interurban electric railways unless operated as a part of a general steam railroad system of transportation or engaged in the general transportation of freight; and
- (d) Any belt-line railroad, terminal switching railroad, or other terminal facility, owned exclusively and maintained, operated, and controlled by any State or political subdivision thereof, shall on or before February 1, 1922, report to the Secretary of the Interstate Commerce Commission, Washington, D. C., the following matters:

1. The amount by which its net railway operating income for the period ended December 31, 1920, was in excess of that percentage of the value of railway property held for and used by it in the service of transportation, established by the foregoing rules, with explanation and details of the manner in which such excess income was computed, or, in the event there was no such excess railway operating income, that fact, with corresponding calculations and details in support of the return.

2. In cases where excess-net railway operating income is reported, a statement of the title of the fund account in which one-half of such excess was placed, when such reserve fund was established, the amount placed in that fund, and how the assets in that fund are represented or held.

3. The amount of the remaining one-half of the excess income as preliminarily computed paid to the Interstate Commerce Commission and when and how such amount was paid. If unpaid, the amount should be paid by remittance to or draft in favor of the Interstate Commerce Commission, transmitted to George B. McGinty, secretary of the Interstate Commerce Commission, Washington, D. C.

4. The value of the railway property of the reporting carrier or carriers with a statement in detail of the manner in which such value is arrived at and a full explanation as to the method in which the values of properties of a group of carriers have been aggregated in cases where property values and income are computed for a system pursuant to the provisions of paragraph (6) of section 15a of the interstate commerce

act. In such cases a full explanation should be given of the reasons why the group of carriers used are treated as under common control, management, and operation.

It is further ordered, That an original report and three copies of the same shall be forwarded to George B. McGinty, secretary, Interstate Commerce Commission, Washington, D. C. Reports shall be prepared in typewritten or printed form, on paper approximately 8½ by 11 inches, with 1½ inches margin at the left side for binding, except as to exhibits, which may be of any convenient size, but which shall be folded to conform to the size of the report.

It is further ordered, That the original reports shall be made under oath, signed and filed on behalf of the carrier by its president, a vice president, auditor, comptroller, or other executive officer having knowledge of the matters therein set forth and duly designated for that purpose by the carrier.

By the commission, division 4:

[SEAL.]

GEORGE B. MCGINTY, Secretary.

[Interstate Commerce Commission, Washington.]

ORDER.

At a session of the Interstate Commerce Commission, Division 4, held at its office in Washington, D. C., on the 16th day of March, A. D. 1922. In the matter of the recovery and payment of excess railway operating income under the provisions of section 15a of the interstate commerce act for the year ended December 31, 1921.

The commission having under consideration the provisions of paragraph (6) of section 15a of the interstate commerce act, reading as follows:

"(6) If, under the provisions of this section, any carrier receives for any year a net railway operating income in excess of 6 per centum of the value of the railway property held for and used by it in the service of transportation, one-half of such excess shall be placed in a reserve fund established and maintained by such carrier, and the remaining one-half thereof shall, within the first four months following the close of the period for which such computation is made, be recoverable by and paid to the commission for the purpose of establishing and maintaining a general railroad contingent fund as hereinafter described. For the purposes of this paragraph the value of the railway property and the net railway operating income of a group of carriers, which the commission finds are under common control and management and are operated as a single system, shall be computed for the system as a whole irrespective of the separate ownership and accounting returns of the various parts of such system. In the case of any carrier which has accepted the provisions of section 209 of this amendatory act the provisions of this paragraph shall not be applicable to the income for any period prior to September 1, 1920. The value of such railway property shall be determined by the commission in the manner provided in paragraph (4)."

It is ordered, That pursuant to the rules and regulations for the determination and recovery of the excess income payable under section 15a of the interstate commerce act, as defined in our order of January 16, 1922, modified as may be necessary in the case of each respondent for the year ended December 31, 1921, each and every carrier by railroad, or partly by railroad and partly by water, within the continental United States, subject to the provisions of the interstate commerce act, excluding—

- (a) Sleeping car companies and express companies;
- (b) Street or suburban electric railways unless operated as a part of a general steam railroad system of transportation;
- (c) Interurban electric railways unless operated as a part of a general steam railroad system of transportation or engaged in the general transportation of freight; and
- (d) Any belt-line railroad, terminal switching railroad, or other terminal facility, owned exclusively and maintained, operated, and controlled by any State or political subdivision thereof, shall on or before May 1, 1922, report to the secretary of the Interstate Commerce Commission, Washington, D. C., the following matters:

1. The amount by which its net railway operating income as defined in paragraph (1) of section 15a of the interstate commerce act, for the year ended December 31, 1921, was in excess of 6 per cent of the value of the railway property held for and used by it in the service of transportation, with explanation and details of the manner in which such excess income was computed, or, in the event there was no such excess railway operating income, that fact, with corresponding calculations and details in support of the return.

2. Where it reports excess net railway operating income, the title of the fund account in which one-half of such excess was placed, the date when such reserve fund was

established, the amount placed in that fund, and how the assets in that fund are represented or held; and the amount of the remaining one-half of the excess income, as preliminarily computed, paid to the Interstate Commerce Commission and when and how such amount was paid. If the latter amount is unpaid, it should be paid by remittance to or draft in favor of the Interstate Commerce Commission, transmitted to George B. McGinty, secretary of the Interstate Commerce Commission, Washington, D. C.

3. The value of such railway property used in earning the income reported for the year ended December 31, 1921, with a statement in detail of the manner in which such value is arrived at and showing the ownership and a general description of such railway property.

4. The foregoing requirements of this order are made subject to the following proviso, that in cases where two or more of said carriers constitute a group under common control and management and operated as a single system, as provided in paragraph (6) above quoted, the foregoing matters shall be reported for the system as a whole, irrespective of the separate ownership and accounting returns of the various parts of such system, but shall also be reported in so far as practicable for each part of the system, and full explanation shall be made as to the method in which the value of properties of a group of carriers have been aggregated and the reasons why the group of carriers used are treated as under common control, management, and operation.

It is further ordered, That an original report and three copies of the same shall be forwarded to George B. McGinty, secretary, Interstate Commerce Commission, Washington, D. C. Report shall be prepared in typewritten or printed form, on paper approximately 8½ by 11 inches, with 1½ inches margin at the left side for binding, except as to exhibits, which may be of any convenient size, but which shall be folded to conform to the size of the report.

It is further ordered, That the original reports shall be made under oath, signed and filed on behalf of the carrier by its president, a vice president, auditor, comptroller, or other executive officer having knowledge of the matters therein set forth and duly designated for that purpose by the carrier.

By the commission, division 4:

[SEAL.]

GEORGE B. MCGINTY, Secretary.

EXHIBIT B.

Class I carriers.

Carrier or groups of carriers comprising a single system, as provided in paragraph (6) of section 15a.	Value of railway property claimed by carrier.		Excess earnings reported by carrier.	Value of railway property used by the commission in its tentative valuation under section 19a.		Excess earnings computed according to tentative valuation as of valuation date given.
	Period ended Dec. 31, 1920.	Year ended Dec. 31, 1921.		Date of valuation, June 30—	Amount. ¹	
Ann Arbor R. R. Co.	\$19,123,546	\$19,373,342	0	1915	\$11,127,277	\$68,119
Manistique & Lake Superior R. R. Co.	1,497,948	1,502,240	0	1915	686,444	1,305
Total system.....	20,621,494	20,875,582	.....	.....	11,813,721	69,424
Athens, Birmingham & Atlantic Ry. Co.	40,935,935	40,021,568	0	1914	25,630,000	.....
Baigor & Aroostook R. R. Co.	30,837,768	31,363,400	0	1916	25,350,084	50,975
Bingham & Garfield Ry. Co.	7,190,647	7,182,065	0	1916	5,896,443	.....
Boston & Maine R. R.	245,250,895	237,392,297	0	1914	234,189,816	.....
Vermont Valley R. R. Co.	.....	2,101,822	0	1914	2,450,000	.....
Sullivan County R. R. Co.	.....	1,421,552	0	1914	2,100,000	.....
York Harbor & Beach R. R. Co.	.....	334,335	0	1914	407,843	.....
St. Johnsbury & Lake Champlain R. R. Co.	.....	4,132,574	0	1916	2,924,120	.....
Montpelier & Wells River R. R. Co.	.....	1,370,537	0	1914	1,925,000	.....
Total system.....	245,250,895	246,753,117	.....	.....	243,906,779	.....

¹ These figures do not include additions and betterments, retirements, or other changes in property since valuation date.

EXCESS EARNINGS OF RAILROADS.

Class I carriers—Continued.

Carrier or groups of carriers comprising a single system, as provided in paragraph (6) of section 15a.	Value of railway property claimed by carrier.		Excess earnings reported by carrier.	Value of railway property used by the commission in its tentative valuation under section 19a.		Excess earnings computed according to tentative valuation as of valuation date given.
	Period ended Dec. 31, 1920.	Year ended Dec. 31, 1921.		Date of valuation, June 30—	Amount.	
Buffalo & Susquehanna R. R. Corporation.	\$15,550,741	\$15,504,923	\$15,906			
Central Vermont Ry. Co.	22,184,322	22,166,416	0	1917	\$22,065,787	
Charleston & Western Carolina Ry. Co.	9,920,289	9,830,092	0	1915	10,509,027	
Augusta & Summerville R. R. Co.		65,532	0	1916	79,671	
Total system.	9,920,289	9,895,624			10,588,698	
Chicago & Eastern Illinois Ry. Co.	91,323,655	89,430,163	0	1915	69,206,753	\$334,775
Chicago, Indianapolis & Louisville Ry. Co.	47,738,810	47,404,572	0	1915	31,495,358	
Chicago, Rock Island & Pacific Ry. Co. (system)	401,263,327	403,331,832	0	1915	335,490,263	
Copper Range R. R. Co.	7,957,302	7,955,753	0	1916	4,610,000	
Delaware & Hudson Co. (system)	118,970,386	123,903,200	0	1916	98,728,801	1,698,824
Detroit & Toledo Shore Line R. R. Co.	6,371,404	6,358,789	150,914			
Duluth, South Shore & Atlantic Ry. Co.	48,545,384	47,901,376	0	1916	17,967,191	
Elgin, Joliet & Eastern Ry. Co.	74,387,466	73,526,059	0	1914	39,049,163	1,289,388
Florida East Coast Ry. Co.	51,654,010	52,856,039	0	1916	47,640,143	
Georgia R. R., lessee organization	14,167,264	14,194,838	0	1916	17,521,976	
Georgia Southern & Florida Ry. Co.	14,815,335	14,587,105	0	1915	9,860,191	
Green Bay & Western R. R. Co. (system)	42,720,333	12,720,333	0	1916	7,264,183	
Gulf & Ship Island R. R. Co.	14,470,327	14,515,364	0	1916	9,036,302	
Central of Georgia Ry. Co.	95,821,423	95,684,345	0	1915	81,872,841	
Kansas City Southern Ry. Co. (system)	105,160,780	105,702,368	0	1914	49,445,907	1,869,823
Lake Superior & Ishpeming Ry. Co. (system)						
Lehigh & New England R. R. Co. (system)	18,966,882	18,671,407	0	1916	7,913,267	241,268
Louisiana Ry. & Navigation Co.	17,554,689	17,464,153	24,508			
	21,670,780	21,982,211	0	1917	10,796,479	
Maine Central R. R. Co.	64,364,206	64,709,688	0	1916	61,091,384	
Portland Terminal Co.	6,914,976	7,199,409	0	1916	8,096,704	
Sandy River & Rangely Lakes R. R.	1,288,223	1,285,681	0	1916	1,359,427	
Bridgton & Saco River R. R. Co.	300,990	304,434		1916	360,563	
Total system.	72,874,395	73,499,272			70,906,078	
Mineral Range R. R. Co.	3,514,800	3,283,147	0	1916	3,879,195	
Minneapolis, St. Paul & Sault Ste. Marie..	195,950,785	205,578,762	0	1916	111,945,828	
Mobile & Ohio R. R. Co.	56,408,487	53,797,941	0	1915	44,462,449	
Nevada Northern Ry. Co.	3,688,730	3,213,096	0	1917	5,325,532	
New Orleans, Great Northern R. R. Co.	16,314,886	16,559,849	0	1916	7,201,388	
New York, New Haven & Hartford R. R. Co.	439,998,432	441,336,414	0	1915	382,797,066	
Central New England Ry. Co.	28,666,905	28,490,286	0	1916	22,589,129	
Total system.	468,665,337	469,832,700			405,386,195	
New York, Ontario & Western Ry. Co.	95,053,287	95,654,057	0	1916	45,051,370	
Norfolk Southern R. R. Co.	34,092,267	34,596,872	0	1914	24,063,840	
Northern Alabama Ry. Co.	5,024,787	4,800,755	0	1916	5,189,429	
Pere Marquette Ry. Co.	122,421,766	125,773,813	0	1915	63,300,242	600,090
Rutland R. R. Co.	25,766,266	25,590,298	0	1916	22,205,821	
St. Louis Southwestern Ry. Co. (system)	108,065,792	137,000,000	0	1915	56,714,295	3,010,173
Spokane International Ry. Co.	5,648,110	5,802,407	0	1917	5,330,039	
Toledo, St. Louis & Western R. R. Co.	43,854,362	44,323,317	0	1916	17,326,263	642,430
Trinity & Brazos Valley Ry. Co.	11,548,533	11,691,061	0	1916	9,064,566	
Ulster & Delaware R. R. Co.	7,941,892	8,202,701	0	1916	6,472,889	
Virginian Ry. Co. (system)	115,824,370	118,347,726	0	1916	55,862,622	2,312,642
Western Pacific R. R. Co.	93,780,246	93,200,543	0	1914	66,730,011	

Excess earnings paid to the commission, none.

EXCESS EARNINGS OF RAILROADS.

9

Class I carriers whose returns do not show any excess earnings based on valuations claimed and in connection with which no tentative valuation has been made under section 15a.

Carrier, or groups of carriers comprising a single system as provided in paragraph (6) of section 15a.	Value of railway property claimed by carrier.	
	Period ended Dec. 31, 1920.	Year ended Dec. 31, 1921.
Alabama & Vicksburg Ry. Co.	\$6,398,112.75	\$6,669,673.19
Louisiana & Mississippi R. R. & Trans. Co.	387,842.00	462,921.75
Vicksburg, Shreveport & Pacific Ry. Co.	10,007,160.00	10,343,785.56
Total system.	16,793,114.75	17,490,380.41
Atchison, Topeka & Santa Fe Ry. (system).	838,092,061.00	873,468,696.00
Atlanta & West Point R. R. Co.	5,503,510.00	5,402,796.00
Atlantic Coast Line R. R. Co.	214,530,440.00	239,388,143.00
Baltimore & Ohio R. R. Co.	697,424,867.00	707,032,851.00
Staten Island Rapid Transit Ry. Co.	9,278,410.00	9,351,052.00
Baltimore & Ohio, Chicago Terminal R. R. Co.	40,415,018.00	40,426,818.00
Sandy Valley & Elkhorn Ry. Co.	5,355,342.00	5,370,045.00
Long Fork Ry. Co.	2,728,171.00	2,832,896.00
Miller's Creek R. R. Co.	184,784.00	182,613.00
Morgantown & Kingwood R. R. Co.	5,364,169.00	5,272,807.00
Hamilton Belt Ry. Co.	96,937.00	96,937.00
Total system.	760,547,678.00	770,615,709.00
Bessemer & Lake Erie R. R. Co.	93,890,432.00	91,628,423.00
Buffalo, Rochester & Pittsburgh Ry. Co.	98,824,554.00	97,780,748.00
Carolina, Clinchfield & Ohio Ry.	64,631,291.00	64,912,636.00
Carolina, Clinchfield & Ohio Ry. of South Carolina.	3,104,849.00	3,105,696.00
Total system.	67,786,140.00	68,018,331.00
Central R. R. Co. of New Jersey.	154,502,265.00	160,000,324.00
Eastern & Western R. R.	188,158.00	189,822.00
New York & Long Branch R. R. Co.	5,564,377.00	5,701,067.00
Total system.	160,254,800.00	165,891,213.00
Chesapeake & Ohio Ry. Co.	312,539,750.00	324,209,313.00
Chicago & Alton R. R. Co.	139,203,026.00	143,880,763.00
Chicago & Northwestern Ry. Co.	458,672,566.00	467,985,778.00
Chicago, St. Paul, Minneapolis & Omaha.	87,307,812.00	88,200,838.00
St. Louis & Bridge Co.	944,316.00	947,867.00
Total system.	546,924,694.00	557,134,483.00
Chicago, Burlington & Quincy R. R. Co. (system).	528,104,640.00	539,932,197.00
Chicago Great Western R. R. Co.	135,058,882.00	134,714,957.00
Chicago, Milwaukee & St. Paul Ry. Co.	675,715,982.00	689,840,070.00
Chicago, Peoria & St. Louis R. R. Co.	8,003,293.00	8,029,325.00
Cincinnati, Indianapolis & Western R. R. Co.	15,461,432.00	14,708,418.00
Colorado & Southern Ry. Co. (system).	119,579,962.00	120,686,452.00
Colorado & Wyoming Ry. Co.	3,926,054.00	3,904,163.00
Delaware, Lackawanna & Western R. R. Co. (system).	255,757,118.00	258,279,370.00
Denver & Rio Grande Western R. R. Co.	190,632,600.00	191,198,332.00
Denver & Salt Lake R. R. Co.	12,794,509.00	12,995,408.00
Northwestern Terminal Ry. Co.	4,703,606.00	4,703,606.00
Total system.	17,498,115.00	17,699,014.00
Detroit & Mackinac Ry. Co.	7,312,752.00	7,572,004.00
Detroit, Toledo & Ironton R. R. Co.	26,229,620.00	25,275,803.00
Duluth & Iron Range R. R. Co.	70,248,453.00	70,744,075.00
Duluth, Massabe & Northern Ry. Co.	118,302,566.00	120,477,511.00
Duluth, Winnipeg & Pacific Ry. Co.	14,683,744.00	13,679,638.00
El Paso & Southwestern Co.	56,521,914.00	56,688,257.00
El Paso R. R. Co. (system).	465,706,940.00	468,903,229.00
Fort Smith & Western R. R.	12,075,374.00	12,446,854.00
Georgia & Florida Ry.	16,504,285.00	16,648,752.00

EXCESS EARNINGS OF RAILROADS.

Class I carriers whose returns do not show any excess earnings based on valuations claimed and in connection with which no tentative valuation has been made under section 19a—Continued.

Carrier, or groups of carriers comprising a single system as provided in paragraph (6) of section 15a.	Value of railway property claimed by carrier.	
	Period ended Dec. 31, 1920.	Year ended Dec. 31, 1921.
Grand Trunk Railway System:		
Atlantic & St. Lawrence R. R. Co.	\$12,178,658.00	\$13,186,778.00
Champlain & St. Lawrence R. R.	72,746.00	94,405.00
Chicago, Detroit & Canada Grand Trunk Junction R. R. Co.	5,798,209.00	5,933,331.00
Cincinnati, Saginaw & Mackinaw R. R. Co.	1,913,977.00	2,042,735.00
Bay City Terminal Ry. Co., Milwaukee, Detroit & Grand Haven Ry. Co.	8,021,318.00	8,829,612.00
Detroit & Huron Ry. Co.	287,708.00	281,668.00
Grand Trunk Milwaukee Car Ferry Co.	570,856.00	578,767.00
Grand Trunk Western Ry. Co.	33,203,667.00	37,757,053.00
Pontiac, Oxford & Northern R. R.	1,411,150.00	1,588,787.00
Toledo, Saginaw & Muskegon Ry. Co.	3,232,810.00	3,235,017.00
Michigan Air Line Ry.	1,860,344.00	1,954,226.00
St. Clair Tunnel Co.	3,751,045.00	3,757,571.00
United States & Canada R. R. Co.	706,152.00	709,988.00
Total system	73,041,640.00	79,979,347.00
Great Northern Ry. Co. system	495,050,845.00	496,177,738.00
Gulf coast lines:		
New Orleans, Texas & Mexico Ry. Co.	17,085,041.00	18,540,962.00
Beaumont, South Lake & Western Ry. Co.	3,232,358.00	3,284,835.00
Orange & Northwestern R. R. Co.	1,231,500.00	1,245,530.00
St. Louis, Brownsville & Mexico Ry. Co.	16,879,481.00	16,852,223.00
New Iberia & Northern R. R. Co.	2,045,255.00	3,002,658.00
Louisiana Southern Ry. Co.	1,530,138.00	1,542,006.00
San Benito & Rio Grande Valley Ry. Co.	1,085,956.00	1,086,278.00
Brownsville & Matamoros Bridge Co.	303,434.00	304,822.00
Houston Belt & Terminal R. R. Co.	2,508,708.00	2,505,944.00
Total system	46,891,991.00	48,464,280.00
Gulf, Mobile & Northern R. R. Co.	24,796,307.00	25,340,178.00
Hocking Valley Ry. Co.	59,610,023.00	59,226,214.00
Illinois Central R. R. Co. system	472,754,832.00	489,700,894.00
International & Great Northern Ry.	45,798,362.00	45,481,322.00
International Ry. Co. of Maine	8,435,037.00	8,474,665.00
Kansas City, Mexico & Orient R. R. Co.	23,721,957.00	22,980,106.00
Kansas City, Mexico & Orient Ry. Co. of Texas	7,111,074.00	6,986,821.00
Total system	30,833,031.00	29,973,019.00
Kansas, Oklahoma & Gulf Ry. Co. system	12,593,619.00	20,470,854.00
Lehigh & Hudson River Ry. Co.	7,113,735.00	8,632,904.00
Lehigh Valley R. R. Co.	232,099,108.00	234,005,083.00
Louisiana & Arkansas Ry. Co.	11,778,554.00	12,272,137.00
Louisville & Nashville R. R. Co.	331,450,408.00	336,922,126.00
Louisville, Henderson & St. Louis Ry. Co.	8,667,405.00	8,701,940.00
Midland Valley R. R. Co.	19,400,556.00	19,732,985.00
Midland Valley & St. Louis R. R. Co.	64,881,820.00	65,297,906.00
Minneapolis & International Ry. Co.	3,734,546.00	3,725,965.00
Minnesota & International Ry. Co.	8,315,404.00	8,640,006.00
Mississippi Central R. R. Co.	18,403,960.00	18,467,014.00
Missouri & North Arkansas R. R. Co.		
Missouri, Kansas & Texas Ry.	191,185,716.00	193,309,001.00
Missouri, Kansas & Texas Ry. of Texas	76,757,305.00	77,072,553.00
Wichita Falls & Northwestern Ry.	7,530,541.00	7,536,858.00
Total system	275,473,562.00	277,938,406.00
Missouri Pacific R. R. Co.	387,900,672.00	393,594,541.00
Arkansas Central R. R. Co.	733,162.00	704,415.00
Coal Belt Electric Ry.	500,077.00	533,645.00
Union Ry. Co.	2,048,089.00	2,089,991.00
Natchez & Southern Ry.	302,929.00	305,372.00
Total system	391,484,929.00	397,117,968.00
Monongahela Ry. Co.	17,188,268.00	17,302,398.00
Montour R. R. Co.	7,983,367.00	7,950,517.00
Nashville, Chattanooga & St. Louis Ry. system	88,593,041.00	90,294,090.00
New Jersey & New York R. R. Co.	3,522,900.00	3,343,548.00
New York Central R. R. Co. system	1,748,372,217.00	1,803,220,597.00
New York, Chicago & St. Louis R. R. Co.	76,294,885.00	78,069,988.00

EXCESS EARNINGS OF RAILROADS.

11

Class I carriers whose returns do not show any excess earnings based on valuations claimed and in connection with which no tentative valuation has been made under section 19a—Continued.

Carrier, or groups of carriers comprising a single system as provided in paragraph (6) of section 15a.	Value of railway property claimed by carrier.	
	Period ended Dec. 31, 1920.	Year ended Dec. 31, 1921.
New York, Susquehanna & Western R. R. Co.	\$38,601,230.00	\$38,652,288.00
Wilkes-Barre & Eastern R. R.	6,000,000.00	6,000,000.00
Macopin R. R. Co.	104,000.00	104,000.00
Susquehanna Connecting R. R.	500,000.00	500,000.00
Hackensack & Lodi R. R. Co.	8,661.00	8,651.00
Lodi Branch R. R. Co.	12,000.00	12,000.00
Total system.	45,225,891.00	45,276,934.00
Norfolk & Western Ry. Co. system.	347,374,243.00	351,900,286.00
Northern Pacific Ry. Co. system.	532,160,634.00	544,535,034.00
Northwestern Pacific R. R. Co.	68,476,467.00	68,354,987.00
Pennsylvania R. R. Co. system.	2,190,461,900.00	2,196,875,259.00
Philadelphia & Reading Ry. Co. system.	263,140,563.00	264,724,950.00
Pittsburg & Shawmut R. R. Co.	13,636,073.00	13,676,958.00
Pittsburg & West Virginia Ry. Co. system.	38,558,045.00	39,511,636.00
Pittsburg & Shawmut Northern R. R. Co.	27,114,780.00	28,808,300.00
Quincy, Omaha & Kansas City R. R. Co.	6,240,476.00	6,292,649.00
Richmond, Fredericksburg & Potomac R. R. Co. system.	31,753,255.00	33,137,000.00
St. Louis-San Francisco Ry. Co.	358,329,016.00	381,633,106.00
West Tulsa Belt Ry.	62,954.00	63,232.00
Birmingham Belt R. R.	1,463,082.00	1,467,643.00
Paris & Great Northern R. R.	1,076,222.00	1,062,802.00
St. Louis, San Francisco & Texas Ry.	3,159,442.00	3,548,884.00
Fort Worth & Rio Grande Ry.	7,536,530.00	7,906,571.00
Brownwood North & South Ry.	288,217.00	288,502.00
Kansas City, Clinton & Springfield Ry.	5,110,275.00	5,152,703.00
Quannah, Acme & Pacific Ry.	1,990,675.00	1,995,809.00
Total system.	378,990,419.00	403,119,317.00
San Antonio & Aransas Pass Ry. Co.	25,422,039.00	25,401,922.00
San Antonio, Uvalde & Gulf R. R.	5,056,550.00	5,250,030.00
Seaboard Air Line Ry. Co.	200,198,652.00	199,590,957.00
Macon, Dublin & Savannah R. R. Co.	3,784,204.00	3,794,206.00
Savannah & Statesboro Ry. Co.	499,404.00	500,239.00
Raleigh & Charleston R. R. Co.	1,117,592.00	1,117,581.00
Marion & Southern R. R. Co.	324,747.00	324,517.00
Chesterfield & Lancaster R. R. Co.	788,065.00	787,385.00
Charlotte, Monroe & Columbia R. R. Co.	116,485.00	116,808.00
Tampa Northern R. R. Co.	1,961,348.00	1,969,807.00
Tampa & Gulf Coast R. R. Co.	1,075,577.00	1,136,036.00
East & West Coast Ry.	786,061.00	788,195.00
Florida Central & Gulf Ry.	788,000.00	794,518.00
Tampa Union Station Co.	256,950.00	256,950.00
Total system.	211,097,145.00	211,186,280.00
Southern Ry. Co.	565,862,153	560,239,833
Alabama Great Southern R. R. Co.	30,379,295	29,974,796
Cincinnati, New Orleans & Texas Pacific Ry. Co.	58,959,173	59,537,485
New Orleans & Northeastern R. R. Co., New Orleans Terminal Co.	35,993,113	34,853,135
Total system.	691,193,734	684,605,249
Northern Pacific Co. system.	1,065,597,462	1,066,831,431
Spokane, Portland & Seattle Ry. Co.	62,666,165	62,568,664
Oregon Trunk Ry.	16,463,267	16,452,076
Oregon Electric Ry. Co.	13,424,015	13,329,486
United Railways Co.	6,280,709	6,300,748
Total system.	98,834,156	98,650,904
Tennessee Central R. R. Co.	19,845,711	19,862,017
Texas & Pacific Ry. Co.	131,204,286	131,119,730
Texas, Georgia & Western Ry. Co.	9,824,677	9,731,262
Union Pacific R. R. Co. system.	688,308,178	790,381,175
Utah Ry. Co.	16,180,621	16,397,061
Utah Ry. Co. system.	220,046,181	221,759,531
Western Maryland Ry. Co.	131,706,720	137,124,298
Western Railway of Alabama	8,964,838	7,094,875
Winning & Lake Erie Ry. Co.	86,063,651	87,400,788

EXCESS EARNINGS OF RAILROADS.

EXHIBIT C.

Other than class I carriers.

Carrier or group of carriers comprising a single system, as provided in paragraph (6) of section 15a.	Value of railway property claimed by carrier.		Excess earnings reported by carrier.	Value of railway property used by the commission in its tentative valuation under section 19a.		Excess earnings computed according to tentative valuation as of valuation date given.	Amount of excess earnings paid to the commission.
	Period ended Dec. 31, 1920.	Period ended Dec. 31, 1921.		Date of valuation June 30—	Amount ¹		
Batesville Southwestern R. R. Co....	\$347,497	\$382,630	\$13,668	.....	.....	.....	\$7,979.00
Bauxite & Northern Ry. Co.....	100,462	100,462	15,958	.....	.....	.....	.....
Brimstone R. R. & Canal Co.....	811,585	811,585	11,549	1918	\$245,486	\$62,529	5,774.70
Campbell's Creek R. R. Co.....	219,181	212,445	13,167	.....	.....	.....	.....
Chicago & Illinois Midland Ry. Co....	4,464,713	4,462,911	86,587	.....	.....	.....	.....
Cisco & Northeastern Ry. Co.....	1,211,088	1,357,074	14,762	.....	.....	.....	.....
Cornwall R. R. Co.....	1,425,739	1,597,677	85,478	.....	.....	.....	.....
Dayton-Goose Creek Ry. Co.....	581,595	699,503	55,433	.....	.....	.....	.....
Detroit Terminal R. R. Co.....	2,571,012	2,602,315	214,524	.....	.....	.....	.....
East Jersey R. R. & Terminal Co....	1,245,796	1,171,833	72,884	1916	475,890	114,701	.....
Fort Worth Belt Ry. Co.....	419,818	910,092	32,866	.....	.....	.....	.....
Genesee & Wyoming R. R. Co.....	1,364,406	1,454,992	203,319	.....	.....	.....	.....
Goshen Valley R. R. Co.....	513,281	513,281	4,813	.....	.....	.....	.....
Gulf & Sabine River R. R. Co.....	.....	359,027	15,702	.....	.....	.....	.....
Ironton R. R. Co.....	3,133,484	3,349,278	30,520	.....	.....	.....	15,238.95
Kinston Carolina R. R.....	218,077	217,979	125	1914	160,841	3,555	.....
Laurinburg & Southern R. R. Co....	698,120	437,694	5,036	.....	.....	.....	2,518.23
Ligonier Valley R. R. Co.....	1,000,000	1,041,560	69,660	.....	.....	.....	.....
Shreveport, Alex. & S. W. Ry. (system).....	873,400	856,789	66,448	.....	.....	.....	.....
St. Joseph Belt Ry. Co.....	914,831	914,694	1,371	.....	.....	.....	685.72
Tionesta Valley Ry. Co.....	572,433	573,303	37,707	.....	.....	.....	.....
Tuckerton R. R. Co.....	514,782	518,777	1,130	1916	503,946	2,020	564.84
Unity Railways Co.....	417,780	421,478	1,842	.....	.....	.....	920.86
Warren & Ouachita Valley Ry. Co....	317,697	316,000	14,679	.....	.....	.....	7,339.26
Warrenton R. R. Co.....	74,039	74,539	3,818	.....	.....	.....	1,909.15
West Virginia Northern R. R. Co....	124,946	174,161	3,596	.....	.....	.....	.....

¹ These figures do not include additions and betterments, retirements, or other changes in property since valuation date.

EXHIBIT D.

Name of carrier.	Excess earnings reported.		Grounds or reasons given by carrier for its failure or refusal to pay over to the commission one-half of the excess earnings reported by it.
	For period ended Dec. 31.	Amount.	
Batesville Southwestern R. R. Co.	1921	\$13,668.00	<p>• • • We are not remitting, however, 50 per cent of the amount in excess of the net amount, as provided by the act of Congress, for the following reasons:</p> <p>First. The Batesville Southwestern Railroad is advised that said act of Congress, known as section 15a, paragraph 6, of the interstate commerce act, is unconstitutional and void, and for this reason does not fix a legal liability against this railroad.</p> <p>Second: The Batesville Southwestern Railroad was not operated by the Government during Federal control, and the act of Congress above referred to only applied to railroads operated under Federal control.</p> <p>Third. That the Batesville Southwestern Railroad did not avail of the guaranty provided under the transportation act.</p>

EXCESS EARNINGS OF RAILROADS.

18

EXHIBIT D—Continued.

Name of carrier.	Excess earnings reported.		Grounds or reasons given by carrier for its failure or refusal to pay over to the commission one-half of the excess earnings reported by it.
	For period ended Dec. 31.	Amount.	
Buffalo & Susquehanna Railroad Corporation.	1920	\$18,905.98	(1) The amount by which the respondent's net railway operating income for the period of four months ended Dec. 31, 1920, was in excess of the proportion for that period of 6 per cent on the value of railway property held for and used by it in the service of transportation was \$18,905.98, as shown by Exhibit A attached. The Interstate Commerce Commission not having prescribed percentages of depreciation which shall be charged on fixed improvements in accordance with the provisions of section 435 of the transportation act, 1920, no deductions have been made for depreciation other than on equipment, in computing the net railway operating income for the period, but necessarily in computing the net railway operating income for that period due allowance will have to be made for depreciation. The Interstate Commerce Commission has adopted a rule prescribing the amount allowable under the guaranty for the six months immediately preceding the four last months of the year. If the commission shall determine that the expenditures for maintenance during the guaranty period were in excess of the amount allowable for that six months, it necessarily follows that any excess over the amount so fixed would have to be considered an expenditure made in the last four months; so that for the two periods the respondent shall receive credit for the actual amount of expenditures for the 10 months of operation by it. It follows that until the allowance for the guaranty period shall have been settled this return must be considered as tentative and not binding on the respondent.
Campbell's Creek R. R. Co.	1921	13,166.80	(2) For the reasons above stated and for other reasons which may involve the validity of the recapture provisions and order, no reserve fund has been created and no remittance has been made to the commission of any part of the net railway operating income of the four last months of 1920. We are advised by counsel that said provision (section 15a) of the interstate commerce act is unconstitutional, null, and void. Our counsel advises us that Hon. Charles E. Hughes gave an opinion to the same effect. We are, however, involuntarily and under protest giving you a financial statement as follows: * * * Involuntarily and under protest we have placed one-half of said excess to a general reserve account, and the same has been used in the current operating expenses of the railroad. We have not remitted said one-half of the excess income because, as advised by counsel, the law providing for such payment is unconstitutional, null, and void.
Chicago & Illinois Midland Ry. Co.	1921 1920	1,028.68 152,716.02	Beg to advise that these returns will be subject to correction * * * due to the fact that we had 250 gondola cars rebuilt in 1920, costing \$339,960.52. None of this amount was charged out in 1920 but the entire amount was put into a suspense account. We have asked permission to adjust our operating expenses for the year 1920 by adding thereto \$100,000, same being that year's proportion of the expense, and also to adjust correspondingly our 1921 figures.
Chgo & Northeastern Ry. Co.	1921	14,762.11	(No grounds or reasons given.)
Cornwall R. R. Co.	1920	85,478.33	Do.
Dayton-Goose Creek Ry. Co.	1920 1921	21,666.24 33,766.90	Now comes Dayton-Goose Creek Ry. Co., hereinafter called "carrier," and, in compliance with the commission's order of Jan. 16, 1922, in the matter of the recovery and payment of excess railway operating income under the provisions of section 15a of the interstate commerce act, files herewith a report of income and earnings and of the other matters referred to in said order, but the carrier states: (1) That said report is not filed voluntarily, but by compulsion and under protest, and for the sole purpose of avoiding prosecutions and possible penalties. (2) That this commission has no lawful or constitutional right to require the carrier to make or file said report for the purposes set out in said order.

EXCESS EARNINGS OF RAILROADS.

EXHIBIT D—Continued.

Name of carrier.	Excess earnings reported.		Grounds or reasons given by carrier for its failure or refusal to pay over to the commission one-half of the excess earnings reported by it.
	For period ended Dec. 31.	Amount.	
Dayton-Goose Creek Ry. Co.—Contd.	.....	.....	<p>(3) That so much of the transportation act, 1920, amending the interstate commerce act, as purports to require the carrier to give up or to pay over to this commission any part of the carrier's earnings or income is unconstitutional and void, for that the enforcement of so much of said act against the carrier would deprive it of its property without due process of law and take its property for public use without just compensation, in contravention of the fifth amendment of the Constitution of the United States.</p> <p>(4) That said order of the commission, of date Jan. 11, 1922, because based and wholly predicated upon section 15a of the interstate commerce act which was added thereto by section 422 of the said transportation act, 1920, is likewise unconstitutional and void for that the enforcement of that portion of said order requiring the carrier to pay over to this commission any part of its earnings or income, would deprive the carrier of its property without due process of law and take its property for public use without just compensation, in contravention of the fifth amendment to the Constitution of the United States.</p> <p>(5) The carrier protests against the accuracy of the preliminary bases prescribed in and by said order of the commission, and all rights are expressly reserved to the carrier to object to any conclusions which may be reached by the commission upon the report filed herewith, and to any report or order made thereon or in connection therewith, and to contest in all proper and legal ways the enforcement of any order based upon said report or any part thereof, or upon said bases prescribed by the commission, and to so contest all efforts of the commission and of the United States of America to require the carrier to pay over to the commission or to any other persons whomsoever, without its consent, any portion of the carrier's earnings, income money, or property.</p> <p>(No ground or reasons given.)</p>
Detroit & Toledo Shore Line R. R. Co.	1920	\$150,914.13	<p>The carrier has not established a reserve fund under the provisions of paragraph (6) of section 15a, because it has not been determined for the period in question that it had any excess net railway operating income within the meaning of said section. Whether or not there was such net railway operating income can be determined only after the commission has ascertained the value of the railway property of the carrier held for and used in the services of transportation.</p> <p>The value (within the meaning of section 15a of the act) of the railway property held for and used by Detroit Terminal R. R. Co. in the service of transportation is not known by the carrier or by the deponent, the same being required to be fixed by the commission in the manner provided in paragraph (4) of said section. The deponent believes that such value should be fixed at an amount greatly in excess of the amount hereinbefore set forth under "1" based on property investment figures or "book values" in accordance with the commission's order.</p> <p>The carrier by its counsel states that the proprietary interest, the Tidewater Oil Co., and its subsidiary, the Tidewater Oil Sales Corporation, intend filing complaint to recover alleged unreasonable freight charges exacted from them; that such complaints will exceed in amount the excess income reported; and that, inasmuch as no substantial defense could be made to such complaints, it is willing to consent to reparation. "In such circumstances," carrier's counsel urges, "I believe that if section 15a were held to apply to the situation, nevertheless, it would be invalid from the point of view that since the act renders carriers amenable to shippers for reparation for unreasonable charges, the result would be to require the carrier to repay the excess to the shipper and also one-half of it into the commission's fund."</p> <p>At the time returns were filed, the requirement was protested on the ground that the section is unconstitutional in any event, and this contention is not waived by the foregoing argument. But it is believed that even if the section might be construed to be constitutional in some cases, it would be inapplicable in the instant case.</p>
Detroit Terminal R. R. Co.	1920 1921	18,749.64 195,775.36	
East Jersey Railroad & Terminal Co.	1921	72,884.90	

EXCESS EARNINGS OF RAILROADS.

15

EXHIBIT D—Continued.

Name of carrier.	Excess earnings reported.		Grounds or reasons given by carrier for its failure or refusal to pay over to the commission one-half of the excess earnings reported by it.
	For period ended Dec. 31.	Amount.	
Port Worth Belt Ry. Co.	1921	\$32,866.26	(No grounds or reasons given.)
Genesee & Wyoming R. R. Co.	1920	93,091.16	That tentative report is filed under protest. In filing the same, the Genesee & Wyoming R. R. Co. does not admit the constitutionality of section 15a of the interstate commerce act, or acknowledge the authority of the Interstate Commerce Commission to require the filing of this report under the provisions of section 15a of the interstate commerce act. On the contrary, it denies the constitutionality of section 15a of the interstate commerce act, and it further denies that the provisions of that section authorized the Interstate Commerce Commission to issue its order of Jan. 16, 1922, as amended Feb. 4, 1922, or to require the filing of this report.
	1921	110,288.12	
Goshen Valley R. R. Co.	1920	4,430.88	Referring to your letter of Dec. 6, directed to Orson P. Rume, auditor of Goshen Valley R. R. Co., the matter has come to my attention as attorney for the company, and I beg to remind you of the return made Nov. 16, 1922, wherein you are advised as to the cost of the railroad and its earnings, and wherein you are advised that this company obligated itself upon its formation to pay 7 per cent interest on the advances made for its construction. This contract was made before the law went into effect by which you seek to require us to pay over the excess of 64 per cent. We decline to be bound by this law in the face of our contract to the contrary. You are, therefore, advised that I have advised the company that it is not bound to perform, as directed by you, nor to make the payments directed by you.
	1921	382.34	
Gulf & Sabine River R. R. Co.	1921	15,702.35	Comes now the Gulf & Sabine River R. R. Co., a Louisiana corporation with its domicile at Fullerton, in Vernon Parish, La., and respectfully represents: That it alleges the illegality of the order of division 4 of your honorable commission of date Jan. 16, 1922, which order was issued in the matter of the recovery and payment of excess railway operating income under the provisions of section 15a of the interstate commerce act, because said order, in its effect, will deprive appearer of its property without due process of law and is thus violative of the Constitution of the United States. That in making the report required by the order above referred to, appearer does not admit the legality of said order, but, on the contrary, denies the same and now specially protests against the requirements that such report be made in any form whatsoever. Now, in the event it should be finally determined that section 15a of said act and the above-mentioned order issued thereunder are legal and binding, then, in the alternative, appearer protests against the making of the report required by said order in the form required and especially protests against the method required by said order to be used in arriving at or computing the profits to be reported in such reports, because such method does not and will not disclose the true profits, nor permit the setting aside of surplus which may be earned in good business years to absorb the losses which accrue in years of business depressions. That interest on bonded and other indebtedness and other fixed necessary charges are as much items of expense as any other operating expense and the denial of permission to deduct from the profits such interest and fixed charges will work an irreparable injury to appearer, is unjust and unreasonable and will deprive it of its property without due process of law. Wherefore, appearer prays that this protest be filed and, upon consideration, that said order be recalled in whole, and, in the alternative, that the requirements thereof be amended so as to permit appearer, in computing its net earnings or profits, to deduct therefrom the amount of interest and other fixed charges which it is required to pay.
Eastern Carolina R. R. Co.	1921	126.53	(No grounds or reasons given.)

STATE OF NEW YORK

IN SENATE

January 1, 1901.

REPORT

OF THE

FILED

NOV 26 1923

WM. R. STANSBURY
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM

NO. 330

DAYTON-GOOSE CREEK RAILWAY COMPANY,
Appellant,

vs.

THE UNITED STATES OF AMERICA, INTERSTATE
COMMERCE COMMISSION, *et al.*,
Appellees.

BRIEF OF APPELLANT FILED IN REPLY TO BRIEF OF
NATIONAL ASSOCIATION OF OWNERS OF RAIL-
ROAD SECURITIES.

FRANK ANDREWS,
ROBERT J. CARY,
ROBERT H. KELLEY,
F. C. NICODEMUS, JR.,
Solicitors for Appellant.

ANDREWS, STREETMAN, LOGUE & MOBLEY,
of Counsel.

IN THE
SUPREME COURT OF THE UNITED
STATES

October Term, 1923.

No. 330

DAYTON-GOOSE CREEK RAILWAY COMPANY, Appellant, <i>vs.</i> THE UNITED STATES OF AMERICA, <i>et al.</i> , Appellees.	}
--	---

APPEAL FROM THE DISTRICT COURT OF THE UNITED
STATES FOR THE EASTERN DISTRICT OF TEXAS.

**BRIEF ON BEHALF OF APPELLANT IN REPLY
TO THE AMICUS CURIAE BRIEF FILED BY
THE NATIONAL ASSOCIATION OF OWNERS
OF RAILROAD SECURITIES.**

Statement.

At the opening of the argument of this appeal this Court granted to the National Association of Owners of Railroad Securities leave to file a brief as *amicus curiae* in support of the constitutionality of the income-appropriation provisions of Section 15a of the Interstate Commerce Act as amended by the Transportation Act, 1920.

From the formal application of the Association for leave to file its brief it appears that the membership of the Association "includes the owners of a very large proportion of the securities of the American railways—probably in excess of 50% principal amount of the entire funded indebtedness of the Class 1 railways of the United States."

Passing note may be made of the fact that this Association thus appears to be interested in the Transportation Act as representing the owners of funded indebtedness of Class 1 railways rather than as representing stockholders. It developed upon one of the hearings before the Senate Committee on Interstate Commerce that the Association represents various life insurance companies, savings banks, national and state banks, trust companies, casualty and surety companies, trust estates, universities and other holders of investment securities, and that it was organized for the purpose of giving representation in the discussion of railroad problems and railroad policies to bondholders who have no voice in the corporate management of the carriers and that it has not solicited stockholders for membership.*

It is apparent from the character of the Association's membership that its attitude respecting the reaction of the income-appropriation provisions of Section 15a upon the affairs of the rail carriers develops through a relation distinct from and in a measure opposed to the interest of the stockholders.

*Hearing before Senate Committee on Interstate Commerce, 67th Congress, First Session, under Senate Resolution 23, Vol. 2, pages 824; 847; 848.

Inasmuch as the Association admits responsibility for "the economic and legal theory of the present rate-making provisions of the Transportation Act, including the excess earnings clause," and attributes the enactment of this legislation to the arguments presented by its own counsel to the Newlands Committee in the fall of 1916, the brief which it now files in this Court commands attention.

We shall, therefore, avail of our privilege to file a brief in reply.

ARGUMENT.

I.

The interdependence between the rate-making provisions and the income-appropriation provisions of Section 15a sought to be established by the Association does not exist.

Throughout the brief of the Association the income-appropriation provisions of Section 15a are treated as an integral and necessarily interdependent part of the alleged rate-making scheme underlying the Transportation Act.

While the historical review and statement of economic conditions developed in the Association's brief undoubtedly disclose the necessity of a more liberal rate policy than antedated the Transportation Act, there is no warrant whatever for the assumption that the income-appropriation provisions are an indispensable part of the Act adopted in pursuance of such policy.

This is at once demonstrated when it is considered that subdivisions (2), (3) and (4) of Section 15a could be repealed without affecting the operation of subdivisions (5) and (6), while subdivisions (5) and (6) could be repealed without affecting the operation of subdivisions (2), (3) and (4).

Apart from this it appears from the brief of the Solicitor General that the question of the constitutionality of subdivisions (5) and (6) of Section 15a was a critical question in Congress, and that the *only* constitutional question seriously considered by Congress related to subdivisions (5) and (6). In the face of this Congress adopted Section 502, declaring that if any clause, sentence, paragraph or part of the Act shall for any reason be adjudged by any court to be invalid, such judgment shall not affect, impair or invalidate the remainder of the Act but shall be confined in its operation to the clause, sentence, paragraph or part of the Act directly involved in the controversy.

This furnishes an unconditional certificate of assurance that these provisions are not essentially interdependent and that the courts may pass judgment upon the income-appropriation provisions unaffected by any apprehension that a declaration of their invalidity as separable provisions of the Act would defeat the intent of Congress.

II.

The underlying vice of the argument in the brief of the Association lies in the assumption that legislative appropriation of private property is consistent with due process of law.

In replying to the argument advanced in the brief of the Association we shall not undertake to deal separately with the twenty-odd main propositions developed by its counsel with manifest care and industry.

Reducing the whole argument to a simple analysis, the Association rests upon one proposition, namely:

That by reason of the necessity of sustaining essential competitive agencies of transportation Congress has authorized and directed a uniform structure of rates in each rate group or rate territory, which rates as between the shipper and all carriers are conclusively presumed to be reasonable, but as between any individual carrier and the Government are conclusively presumed to be unreasonable if as the result of twelve months operation such carrier shall earn a net railway operating income in excess of the statutory maximum of 6% fixed by the Act, and that any income earned by such carrier in excess of such statutory maximum is not property protected by the Fifth Amendment.

Thus it is stated and reiterated throughout the brief that "Congress may foreclose the reasonableness and legality of a rate as to a shipper but leave the question open as to the Government" (Association's brief, pages 22, 33, 34, 96-97, 99-100).

The answer to this argument is threefold:

(a) The Association rests upon an erroneous assumption that as between the shipper and the carrier a judicial inquiry as to the reasonableness and legality of the rates producing the alleged excessive income has been foreclosed by Congress.

(b) The Association rests upon an erroneous assumption that Congress consistently, with due process of law, may as between the carrier and the Government foreclose a judicial inquiry as to the reasonableness of the carrier's rates by creating a *conclusive* presumption that rates producing a net railway operating income in excess of a fixed percentage of the value of the carrier's railway property are *pro tanto* unreasonable.

(c) The Association rests upon an erroneous assumption that Congress consistently, with due process of law, may foreclose a judicial inquiry as to the reasonableness of the rate of return which the carrier is permitted to earn upon its railway property.

We shall discuss these three propositions briefly in their order:

(a) *The Association rests upon an erroneous assumption that as between the shipper and the carrier a judicial inquiry as to the reasonableness and legality of the rates producing the alleged excessive income has been foreclosed.*

At the outset we challenge the basic proposition that a rate may be reasonable for the shipper to pay and unreasonable for the carrier to accept.

To state the proposition is to utter an obvious solecism.

The rate must be reasonable both as to the shipper and the carrier, or unreasonable both as to the shipper and the carrier; it cannot be reasonable as to one and unreasonable as to the other.

Moreover, we insist that every dollar which a carrier earns upon a reasonable schedule of rates is the carrier's private property and is protected as such by the Fifth Amendment.

If, however, it be assumed that "Congress may foreclose the reasonableness and legality of a rate as to a shipper but leave the question open as to the Government", if becomes pertinent to inquire whether it has done so by the Transportation Act, 1920.

Clearly it has not.

On the contrary, by subdivision (17) of Section 15a Congress has expressly preserved unimpaired the shipper's right of reparation for excessive charges, subject to the single condition that the shipper shall not be entitled to recover upon the sole ground that a particular rate may reflect a proportion of excess income to be paid by the carrier to the Commission. That is to say, the fact that the carrier has earned excess income subject to appropriation under subdivisions (5) and (6) of Section 15a shall not be conclusive evidence that a particular rate is unreasonable and a recovery may not be had against the carrier upon that sole ground. If, however, evidence of the fact that excess income has been earned by the carrier is supplemented by even a scintilla of additional or extrinsic evidence, it may be held sufficient to establish the shipper's right to reparation.

Thus the carrier is exposed to the double jeopardy of (a) appropriation of excess income by the Government under subdivisions (5) and (6) of Section 15a, and (b) a claim by the shipper for reparation under subdivision (17) of Section 15a.

The Dayton-Goose Creek Company is peculiarly subject to this hazard. The bulk of its business is the transportation of crude and refined oil in interstate commerce under rates established by the Interstate Commerce Commission under subdivision (2) of Section 15a. It appears that there is now pending with the Interstate Commerce Commission, Docket No. 14122, a complaint by Lubright Refining Company in which reparation is sought to be recovered on account of the assessment and collection upon certain shipments of crude oil from Goose Creek, Texas, to East St. Louis, Illinois, which moved on dates between March 1, 1920, and December 31, 1921, on rates alleged to have been unjust, unreasonable, unlawful and excessive (Record 50-51). As the reparation claim of this one shipper amounts to \$1200.00 it is evident that if this claim is allowed and the carrier is called upon to respond to other shippers having like claims, it will be mulcted in an aggregate amount greatly exceeding the amount of its alleged excess income for the years 1920 and 1921.

The fact that the carrier's income is thus placed in jeopardy of double appropriation not only strikes at the foundation of the Association's argument but alone demonstrates that subdivisions (5) and (6) of Section 15a ignore the basic requirements of due process of law.

- (b) *The Association rests upon an erroneous assumption that Congress consistently, with due process of law, may as between the carrier and the Government foreclose a judicial inquiry as to the reasonableness of the carrier's rates by creating a conclusive presumption that rates producing a net railway operating income in excess of a fixed percentage of the value of the carrier's railway property are pro tanto unreasonable.*

In the opening paragraph of the brief filed by the Association its counsel characterizes Section 15a of the Transportation Act as an act "relating to the regulation or reduction of excess carrier income gratuitously and conditionally allowed the carrier, by requiring one-half of such excess, *when ascertained and defined in pursuance of due process* (our italics), to be paid into a general fund to be administered by the Commission as a by-product of effective rate regulation in the general public interest in transportation, and thus essentially in the interest of the shipping public which has paid the excess."

While at the very outset the Association thus admits that excess income is subject to appropriation only when its character as excess income has been "ascertained and defined in pursuance of due process," it assumes that a bald legislative declaration satisfies this fundamental constitutional requirement.

This is the precise point at which our arguments diverge.

We reiterate our conviction that the alleged excess income of the Railway Company cannot be taken away, either in whole or in part, on the

theory that it is excess income, without a judicial ascertainment and determination of that underlying fact.

Congress has no more right to say that railway operating income in excess of a fixed amount shall be conclusive evidence of excessive reward for transportation service or excessive rates for transportation service than it had to say that the courts in ascertaining the condemnation value of the Monongahela Bridge could not take into consideration the value of the Bridge Company's franchise.

As Mr. Justice Brewer said in the Monongahela case:*

"It does not rest with the public, taking the property, through Congress or the legislature, its representative, to say what compensation shall be paid, or even what shall be the rule of compensation. The Constitution has declared that just compensation shall be paid, and the ascertainment of that is a judicial inquiry."

By a line of decisions of this Court the Dayton-Goose Creek Company is entitled under the protection of due process to receive as compensation for its transportation service on each class of business the cost of that service plus a reasonable reward.**

If by reason of excessive rates or otherwise the Railway Company during the years 1920 and 1921

**Monongahela Navigation Company v. United States*, 148 U. S. 312; 327.

***Vandalia Railway Company v. Schnell*, 255 U. S. 139.
Northern Pacific Railway Company v. North Dakota, 236 U. S. 585.
Norfolk & Western Railway Company v. West Virginia, 231 U. S. 605.

has received for its transportation service more than a reasonable reward on each class of its business, it is, to the extent that such reward is excessive, liable to respond to shippers. This liability, as we have already shown, is expressly kept alive by subdivision (17) of Section 15a.

In any action or proceeding for reparation brought by a shipper under subdivision (17) the *sine qua non* of a recovery must be a judicial ascertainment and determination that the carrier's reward is unreasonable and excessive.

Certainly no one would contend that in such a case Congress consistently, with due process, could fetter the judiciary in its decision of such question by a binding pronouncement that a specified rate of return upon the value of the carrier's property shall be accepted as conclusive evidence that the carrier has received an unreasonable and excessive reward.

Much less can it do so when it seeks to make the United States the beneficiary of the alleged excessive reward and to cover it into the public Treasury.

Again we refer to and invoke the Monongahela Bridge case and respectfully submit that the right of Congress "to constitute itself the judge in its own case, to determine what is the 'just compensation' it ought to pay therefor, or how much benefit it has conferred upon the citizen by thus taking his property without his consent, or to extinguish any part of such 'compensation' by prospective conjectural advantage, or *in any manner* to interfere with the just powers and province of courts and juries in administering right and justice, cannot for a moment be admitted or tolerated under our Constitution."

- (c) *The Association rests upon an erroneous assumption that Congress consistently, with due process of law, may foreclose a judicial inquiry as to the reasonableness of the rate of return which the carrier is permitted to earn upon its railway property.*

In the appendix of the brief of the Association reference is made to an article by Charles W. Bunn, Esq., appearing in the Yale Law Journal, January, 1923. In this article, which is quoted at page 47 of the Solicitor General's brief, Mr. Bunn says:

"If a carrier's rates may be made with reference to its prosperity lower than those of other carriers, and if no carrier can insist as an absolute legal right on receiving more than a fair return on the value of its property, it would seem that there can be no violation of the Constitution in the mere recapture of so-called earnings made after the act was on the statute books, provided that after the recapture the carrier is left with a reasonable return on the value of its property."

The statement that no carrier can insist as an absolute legal right on receiving more than a fair return on the value of its property runs counter to the decisions of this Court already cited holding that irrespective of the return on the value of the carrier's property it is entitled to receive cost plus a reasonable reward on each and every class of its business.

Apart, however, from this plain defect in his major premise Mr. Bunn, as well as counsel for the Association, clearly overlook the fact that Congress has no power under the Constitution to determine what shall constitute a fair return upon the value of railway property.

This question is non-legislative and essentially judicial.

Here again the statute invades the judicial function.

Subdivisions (5) and (6) of Section 15a clearly involve a legislative declaration that 6% shall constitute a just and reasonable return upon the value of railway property at all times, in all places and under all conditions. To permit Congress to enforce this declaration would undermine a principle of constitutional law which has stood unchallenged since the Granger cases were overruled by this Court in *Chicago, Milwaukee & St. Paul Railway Company v. Minnesota*.*

As late as June 11, 1923, this Court asserting the judicial character of this question under the Constitution annulled a finding of a State Commission that 6% constituted a fair return upon the value of the property of a public utility located in the State of West Virginia.**

Under this decision it is manifest that many, if not all, of the carriers engaged in rail transportation are entitled to complain of the 6% return as confiscatory. It is true that the bill of complaint of the Dayton-Goose Creek Company does not allege specifically that the 6% return is confiscatory as to it. The bill does, however, allege that the income-appropriation clauses of Section 15a operate as "a taking of complainant's property for public use without just compensation and in truth and in fact without any compensation of any character whatsoever and without due process of law" (Record, page 8).

*134 U. S. 418.

***Bluefield Waterworks & Improvement Company v. Public Service Commission of the State of West Virginia, et al.*

The bill of complaint is accurately characterized in the brief of the Solicitor General as a proceeding "in the nature of a demurrer to Section 422 of the Transportation Act of 1920." Clearly, therefore, all questions as to the constitutionality of the statute *on its face* arise upon the Dayton-Goose Creek Company's bill, including the question as to the validity of the 6% return as applied to all carriers throughout the United States, because unless the 6% return can be held good as to all carriers it cannot be held good as to any carrier. To hold otherwise would produce intolerable inequalities.

To illustrate:

Carrier "A" owning a railway located in the State of Nebraska where 8% appears to be the minimum constitutional return*, actually earns 15%. This carrier alleges and proves that 6% is confiscatory as to it and as the result it must be permitted to retain the whole of its income amounting to 15%.

Carrier "B" owning a railway located in the State of New York where at one time 6% was held to be the proper rate of return for a public utility having a peculiarly favorable position**, actually earns 8%. This carrier alleges that the 6% return is confiscatory as to it, but fails to establish that fact and as the result is required to surrender 1% of its income to the United States.

It would be clearly inadmissible to attempt to avoid these inequalities by commencing the income-appropriation at the level of actual confis-

**Lincoln Gas & Electric Company v. Lincoln*, 250 U. S. 256.

***Wilcox v. Consolidated Gas Company*, 212 U. S. 19.

cation in the case of those carriers establishing a constitutional right to a return above 6%. The statute provides no machinery for such appropriation and to read into the statute a provision permitting it, would reconstruct it. Moreover, it appears by reference to subdivision (3) of Section 15a that the statute was drawn upon the theory that the level of confiscation is at a point below 6% and it is not, therefore, the purpose of Congress to commence income-appropriation at that exact level.

As we view it, there can be but one question, namely: Is the 6% return a constitutional and valid return as to every carrier in the United States? If this question is answered in the negative then we submit that these provisions of the statute must be declared unconstitutional.

Under existing economic conditions the 6% rate is clearly confiscatory as to many carriers, if not all carriers. We attach as an appendix a list of railroad stocks listed on the New York Stock Exchange showing the yield basis determined from quotations published November 2, 1923. It is highly significant that practically all of the common stocks on the list sell on higher interest bases than 6%. The common stock of the Union Pacific is upon a 7.68% basis; that of the Pennsylvania Railroad Company upon a 7.1% basis; that of the New York Central upon a 6.81% basis, and so throughout the list. With these prime railroad stocks selling on such bases is it conceivable that any carrier in a proper judicial inquiry would fail to condemn the 6% rate? However this may be, the fact that the statute fixes an inflexible rate applicable to all carriers and makes no provision for a judicial inquiry as to the reasonableness of the

rate so fixed must necessarily undermine the statute as contrary to the fundamental principles of due process of law.

The foregoing argument has proceeded upon the assumption that subdivisions (5) and (6) of Section 15a are a regulation of commerce.

This assumption is, however, one which cannot be indulged.

The true character of a statute must be determined by its actual and not its theoretical reaction; that is, by the test of phenomena that can be observed.

What, then, is observable under these provisions of the statute?

There is no observable reaction upon the transportation rates established under the Act. Rates remain the same regardless of the operation of the provisions for the appropriation of excess income.

There is no observable reaction upon interstate commerce, nor upon "the means by which commerce is carried on."* Regardless of these provisions the agencies of commerce operate precisely as before.

There is but one phenomenon which is observable and that is the reduction by direct appropriation of the income of carriers engaged in interstate commerce. That is to say, the statutory provisions here drawn into question limit income, a product of commerce, but do not regulate commerce itself. In actual operation, therefore, these contested provisions relate to a subject as to which Congress is destitute of regulatory power.

Nor can this conclusion be altered by calling

**Hammer v. Dagenhart*, 247 U. S. 251.

the appropriated income "a by-product of effective rate regulation" (Association's Brief, p. 2).

In his celebrated opinion in *Munn v. Illinois*** Chief Justice Waite points out the objects to which the regulatory power of government extends. He shows that in England from time immemorial and in this country from its first colonization it has been the practice, in order to protect the public from unreasonable and improper charges, to regulate the rates of ferries, common carriers, hackmen, bakers, millers, wharfingers, innkeepers and a variety of other activities.

In all these services a uniform rate structure is just as important and just as essential as it is in the rail transportation service.

If, then, the income-appropriation provisions of the present Act are sustained on the legal and economic theory developed by the Association, it is obvious that the State of Illinois, putting into effect a uniform rate schedule applicable to the grain elevators which were before this Court in *Munn v. Illinois*, is at liberty to appropriate "as a by-product of effective rate regulation" all operating income of a particular elevator in excess of the level of actual confiscation. It is equally true that the income of every innkeeper in the State of New York above the level of plain confiscation is by like token subject to appropriation by the State of New York.

The fallacy of the legal and economic theory advanced in the brief of the Association is that counsel ignore the fact that the one purpose and object of governmental rate regulation is to protect the public against improper charges by securing just and reasonable rates and that when this

**94 U. S. 113.

is done the Government has performed its function and exhausted its power.

Whatever a rail carrier or grain elevator or innkeeper or any other servant of the public can earn under a system of rates so established by the proper governmental authority, is no more than a just and reasonable reward for its service and is private property protected by the Fifth Amendment.

All of which is respectfully submitted,

FRANK ANDREWS,
ROBERT J. CARY,
ROBERT H. KELLEY,
F. C. NICODEMUS, JR.,
Solicitors for Appellant.

ANDREWS, STREETMAN, LOGUE & MOBLEY,
Of Counsel.

APPENDIX

List of Railroad Stocks Listed on New York Exchange Showing Yield
Basis Determined from Quotations Published November 2, 1923.

	RATE	PRICE	YIELD
Atchison, Topeka & Santa Fe	6%	97	6.2%
Atchison, Topeka & Santa Fe Pfd.	5%	88	5.7%
Atlantic Coast	7%	112½	6.2%
Baltimore & Ohio	5%	58¾	8.½%
Baltimore & Ohio 4% Pfd.		58	6.9%
Buffalo, Rochester & Pitts.	5%	54	9.3%
Canadian Pacific	10%	147	6.7%
*Chesapeake & Ohio Com.	4%	73⅛	5.½%
Chesapeake & Ohio Pfd.	6½%	98½	6.6%
Colorado Southern Ry.	3%	19	15.8%
Colorado Southern 1st Pfd.	4%	49	8.1%
Colorado Southern 2nd. Pfd.	4%	35	11.4%
Chicago & Northwestern	5%	62	8.%
Chicago & Northwestern Pfd.	7%	104	6.7%
Chicago, R. I. & Pac. Pfd.	6%	66	9.%
Chicago, R. I. & Pac. Pfd.	7%	77	9.1%
C. C. C. & St. L.	4%	98½	4.06%
Delaware & Hudson Co.	9%	109¾	8.2%
Del. Lacka. & West.	12%	114⅞	10.4%
Great Northern Pfd.	5%	55⅞	8.94%
Ill. Cen.	7%	103¼	6.77%
Ill. Cen. Pfd.	6%	107¼	5.6%
Ill. Cen. Pfd. W. I.	6%	103½	5.8%
Ill. Cen. Leased Lines	4%	70½	5.6%
Kan. City Pfd.	4%	51½	7.7%
Lehigh Valley	3½%	61	5.¾%
Louisville & Nashville	5%	87	5.¾%
M. St. Paul S. S. M.	4%	50	8.%
N. Ore. T. & M.	7%	88½	7.9%
New York Central	7%	101½	6.81%

	RATE	PRICE	YIELD
New York C. & St. Louis Pfd.	6%	87 $\frac{3}{4}$	6.83%
New York C. & St. Louis	6%	76	7.89%
Norfolk & Western	7%	104 $\frac{3}{4}$	6.68%
Norfolk & Western Pfd.	4%	72 $\frac{1}{2}$	5.1 $\frac{1}{2}$ %
*Penn. R. R.	6%	41 $\frac{3}{4}$	7.1%
Pere Marquette	4%	41 $\frac{1}{4}$	9.6%
Pere Marquette Pfd.	5%	58	8.62%
Pere Marquette Pr. pf.	5%	70	7.1%
Pitts. & West Virginia Pfd.	6%	86	6.98%
Pullman Company	8%	115 $\frac{3}{4}$	6.9%
St. Louis Southwestern Pfd.	5%	56 $\frac{1}{4}$	8.8%
Southern Pacific	6%	86 $\frac{1}{8}$	6.26%
Southern Railway Pfd.	5%	66 $\frac{7}{8}$	7.4%
Union Pacific	10%	130	7.68%
Union Pacific	4%	72	5.1 $\frac{1}{2}$ %
Western Pacific	6%	56	10.7%
*Reading	8%	76 $\frac{5}{8}$	10.4%
Reading Pfd. 1	4%	53 $\frac{3}{4}$	7.4%
Reading Pfd. 2	4%	53	7.4%

NOV 12 1923

WM. R. STANBURY

Supreme Court of the United States,

OCTOBER TERM, 1923.

No. 330.

DAYTON-GOOSE CREEK RAILWAY COMPANY,

Appellant,

v/s.

THE UNITED STATES OF AMERICA, THE INTERSTATE COMMERCE
COMMISSION, AND RANDOLPH BRYANT, UNITED STATES DISTRICT
ATTORNEY FOR THE EASTERN DISTRICT OF TEXAS.

APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES FOR THE
EASTERN DISTRICT OF TEXAS.

B R I E F

ASSERTING UNCONSTITUTIONALITY OF PARAGRAPHS (5) AND (6) ET SEQ.
OF SECTION 15a, INTERSTATE COMMERCE ACT.

JOSEPH PAXTON BLAIR
EDGAR H. BOLES
JOHN F. BOWIE
ROBERT J. CARY
HENRY W. CLARK
HERBERT FITZPATRICK
LAWRENCE GREER
W. S. HORTON

WILLIAM S. JENNEY
E. W. KNIGHT
RICHARD V. LINDABURY
WILL H. LYFORD
SAMUEL W. MOORE
WILLIAM CHURCH OSBORN
WINSLOW S. PIERCE
HENRY V. POOR
JOHN H. AGATE
CARL A. DE GERSDORFF

AS Amici Curiae.



INDEX

	PAGE
STATEMENT	1
POINT I. The provisions of the statute appropriating a part of the net railway operating income, and restricting the use of a further part, are not a regulation of interstate commerce, but a direct confiscation of carriers' property and invasion of their property rights in violation of the Fifth Amendment.....	
(a) It was the avowed purpose of the income-appropriation provisions to regulate the railway operating income of carriers, not by a regulation of their rates, but by taking from them a portion of their income, arbitrarily declared by the Act to be excessive.....	4 8
(b) Net income realized from operations in interstate commerce is not a part of commerce and the power to regulate interstate commerce does not include the regulation of such net income.	12
(c) The net income which is the subject of the income-appropriation provisions is the unqualified property of the carriers, and evidences elements of value inherent in their railroads. A taking of the income is a confiscation not only of the amount in money so taken but also of a part of the value of the railroads themselves.....	18
1. The net income is earned from rates which must be presumed to be reasonable, and so is absolute property.....	19
2. The net income evidences elements of value which are an essential part of the railroad property.....	24

II

	PAGE
(d) The statutory declarations that the income to be appropriated is excess income and that it is held in trust are not competent to qualify the title of the carriers thereto.....	28
(e) This attempted appropriation of income is not an indirect or consequential result of any legitimate exercise of Congressional power, but is a direct confiscation of property.....	33
(f) The allocation of a part of the net railway operating income to a reserve fund and the restriction upon the use of such fund by the carrier amount in legal effect to a deprivation of property without due process, equally with the complete appropriation of a portion of the net railway operating income.....	37
(g) The income-appropriation provisions cannot be sustained on the theory that their result is equivalent to a result which might be obtained by prescribing different rates for different roads	41
(h) The <i>New England Divisions</i> case is plainly distinguishable	48
POINT II. The income-appropriation provisions cannot be sustained as a regulation of rates.....	52
(a) Considering the income-appropriation provisions as attempted rate regulation on the theory of a seizure of the proceeds of rates impliedly declared to be unreasonable, they are void because of their want of due process of law, in that the amount of net income is arbitrarily made the sole and conclusive measure of the unreasonableness of the rates.....	52
(b) But the income-appropriation provisions do not purport to be and are not a regulation of rates.	76

III

	PAGE
(c) To construe the income-appropriation provisions as a regulation of rates would do violence to the whole theory upon which rate regulation rests	86
(d) The income-appropriation provisions do not acquire the character of a regulation of rates by reason of any interdependence between them and those provisions of the same section which are concededly a regulation of rates..	89
POINT III. The income-appropriation provisions cannot be sustained as an exercise of the taxing power....	93
(a) The provisions in question do not purport to be an exercise of the power of taxation.....	94
(b) But even if the appropriation of income were labeled as a tax law it would be void because its real purpose, ascertainable from the Act itself, is the limitation of the amount of income which a carrier shall be entitled to retain, an object not within the power of Congress..	98
(c) This appropriation cannot be sustained as a contribution imposed, incidentally to the commerce power, to create the fund called the general railroad contingent fund, as a burden which the industry should bear.....	103
APPENDIX. Text of Section 15a, Interstate Commerce Act.	119

IV

CASES CITED.

	PAGE
<i>Adair v. U. S.</i> , 208 U. S. 161.....	14, 30
<i>Adkins v. Children's Hospital</i> , 261 U. S. 525.....	115
<i>Advances in Rates</i> , 20 I. C. C. 243.....	81
<i>Assaria State Bank v. Dolley</i> , 219 U. S. 121.....	109
<i>Atlantic Coast Line v. N. C. Corp. Com.</i> , 206 U. S. 1....	57
<i>Bailey v. Drexel Furniture Co.</i> , 259 U. S. 20.....	98
<i>Bedford v. U. S.</i> , 192 U. S. 217.....	33
<i>Bluefield Water Works & Improvement Co. v. P. S. Com.</i> , — U. S. —.....	7
<i>Branson v. Bush</i> , 251 U. S. 182.....	38
<i>Buchanan v. Warley</i> , 245 U. S. 60.....	38
<i>Canada Southern Ry. Co. v. International Bridge</i> , 8 App. Cases 723.....	51, 67, 74
<i>Chicago, Burlington & Quincy v. Drainage Com'rs.</i> , 200 U. S. 561.....	29, 34
<i>Chicago, Burlington & Quincy R. R. Co. v. Iowa</i> , 94 U. S. 155.....	42
<i>Chicago & Grand Trunk Railway Co. v. Wellman</i> , 143 U. S. 339.....	43
<i>Chicago, Milwaukee & St. Paul R. R. Co. v. Tompkins</i> , 176 U. S. 167.....	7, 31
<i>Chicago, Milwaukee & St. Paul R. R. Co. v. Wisconsin</i> , 238 U. S. 491.....	57
<i>Child Labor Tax Case</i> , 259 U. S. 20.....	29
<i>City of Spokane v. Northern Pacific Ry. Co.</i> , 15 I. C. C. 376	81
<i>Cleveland, C. C. & St. L. Ry. Co. v. Backus</i> , 154 U. S. 439	38
<i>Coppage v. Kansas</i> , 236 U. S. 1.....	39
<i>Cotting v. Kansas City Stock Yards</i> , 183 U. S. 79.....	59
<i>Covington Turnpike Co. v. Sandford</i> , 164 U. S. 578....	42, 68
<i>Darnell v. Edwards</i> , 244 U. S. 564.....	44
<i>Dayton-Goose Creek Ry. Co. v. U. S.</i> , 287 Fed. 728....	94
<i>Delaware, Lackawanna & Western R. R. Co. v. Yurkonis</i> , 238 U. S. 439.....	14
<i>Detroit & Mackinac Ry. Co. v. Mich. R. R. Com.</i> , 171 Mich. 335.....	75
<i>Dow v. Beidelman</i> , 125 U. S. 68.....	43

	PAGE
Employers' Liability Cases (First), 207 U. S. 463.....	13
Employers' Liability Cases (Second), 223 U. S. 1.....	12
Ex Parte 74, Increased Rates, 1920, 58 I. C. C. 220.....	21, 49
Future Trading Act Case, 259 U. S. 44.....	98
Galveston, Harrisburg & San Antonio Ry. Co. v. Texas, 210 U. S. 217.....	29
Gibson v. U. S., 166 U. S. 269.....	33
Great Northern Ry. Co. v. Minnesota, 238 U. S. 340...	40
Hammer v. Dagenhart, 247 U. S. 251.....	14, 29
Head Money Cases, 112 U. S. 580.....	104
Hill v. Wallace, 259 U. S. 44.....	98
Holden v. Hardy, 169 U. S. 366.....	39
Holmes & Hallowell Co. v. Gt. Nor. Ry. Co., 37 I. C. C. 627	75
Hooker v. I. C. C., 188 Fed. 242.....	70
Interstate Commerce Commission v. B. & O. R. R. Co., 145 U. S. 263.....	20
Interstate Commerce Commission v. Stickney, 215 U. S. 98	57
Interstate Commerce Commission v. U. P. R. R. Co., 222 U. S. 541.....	42, 69
Investigation & Suspension Docket No. 26, 22 I. C. C. 604	23, 75
Kindel v. N. Y., N. H. & H. R. R. Co., 15 I. C. C. 555..	81
Lake Shore & Mich. Southern Ry. Co. v. Smith, 173 U. S. 684.....	55, 57, 86
Lincoln Gas Co. v. Lincoln, 250 U. S. 256.....	7, 31
Louisiana Ry. & Nav. Co. v. Railroad Com., 131 La. 387.	75
McCray v. U. S., 195 U. S. 27.....	102
M'Culloch v. Maryland, 4 Wheat. 316.....	102
Maximum Rate Case, 167 U. S. 479.....	20
Minneapolis, St. P. & S. St. M. Ry. Co. v. Wis. R. R. Com., 136 Wis. 146.....	75
Minnesota Rate Cases, 230 U. S. 352.....	27, 44
Missouri Pacific Ry. Co. v. Nebraska, 217 U. S. 196....	55
Monongahela Navigation Co. v. U. S., 148 U. S. 312....	31, 33
Mountain Timber Co. v. Washington, 243 U. S. 219....	109
Munn v. Illinois, 94 U. S. 113.....	60

VI

	PAGE
New England Divisions Case, 261 U. S. 184.....	5, 17, 48
New York Central R. R. Co. v. White, 243 U. S. 188	110, 112, 115
Noble State Bank v. Haskell, 219 U. S. 104.....	108
Norfolk & Western Ry. Co. v. West Virginia, 236 U. S. 605	57
Northern Pacific Ry. Co. v. North Dakota, 236 U. S. 585.	54
Norwood v. Baker, 172 U. S. 269.....	30
Oklahoma v. Kansas Natural Gas Co., 221 U. S. 229....	40
Peck v. Lowe, 247 U. S. 165.....	17-19
Pennsylvania R. R. Co. v. Towers, 245 U. S. 6.....	57
Philadelphia S. S. Co. v. Pennsylvania, 122 U. S. 326....	16
Proposed Advances in Freight Rates, 9 I. C. C. 382.....	80
Railroad Commission Cases, 116 U. S. 307.....	22
Railroad Commission of Iowa v. Illinois Central R. R. Co., 20 I. C. C. 181.....	74
Railroad Commission of Texas v. Houston & Texas Cen- tral, 90 Tex. 340.....	75
Reagan v. Farmers' Loan & Trust Co., 154 U. S. 362....	22, 69
Receivers & Shippers Assn. v. C., N. O. & T. P. Ry. Co., 18 I. C. C. 440.....	72, 81
San Diego Land and Town Co. v. National City, 174 U. S. 739.....	28
San Joaquin Co. v. Stanislaus County, 233 U. S. 454...	28
Seaboard Air Line v. U. S., 261 U. S. 299.....	31
Shallenberger v. First State Bank, 219 U. S. 114.....	109
Smyth v. Ames, 169 U. S. 466.....	22, 85
Southern Pacific Co. v. I. C. C., 219 U. S. 433.....	57
Southern Railway Co. v. St. Louis Hay Co., 214 U. S. 297	57
Texas & Pacific Ry. Co. v. Abilene Cotton Oil Co., 204 U. S. 426.....	20
Transportation Co. v. Chicago, 99 U. S. 635.....	33
Transportation Co. v. Parkersburg, 107 U. S. 691.....	61
Trier v. Chicago, St. Paul, M. & O. Ry. Co., 30 I. C. C. 352	75
Truax v. Corrigan, 257 U. S. 312.....	66

VII

	PAGE
Union Bridge Co. <i>v.</i> U. S., 204 U. S. 364.....	33
Union Pacific R. R. Co. <i>v.</i> Kansas Pub. Util. Com., 95 Kas. 604.....	75
United Mine Workers <i>v.</i> Coronado Co., 259 U. S. 344...	14
United States <i>v.</i> Doremus, 249 U. S. 86.....	102
United States Glue Co. <i>v.</i> Town of Oak Creek, 247 U. S. 321	15
Veazie Bank <i>v.</i> Fenno, 8 Wall. 533.....	102
Wilcox <i>v.</i> Consolidated Gas Co., 212 U. S. 19.....	22, 28
Wisconsin R. R. Com. <i>v.</i> C. B. & Q. R. R. Co., 257 U. S. 563.....	4

Supreme Court of the United States,

OCTOBER TERM, 1923.

No. 330.

DAYTON-GOOSE CREEK RAILWAY
COMPANY,

Appellant,

vs.

THE UNITED STATES OF AMERICA,
THE INTERSTATE COMMERCE COM-
MISSION, and RANDOLPH BRYANT,
UNITED STATES DISTRICT ATTOR-
NEY FOR THE EASTERN DISTRICT
OF TEXAS.

APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES FOR
THE EASTERN DISTRICT OF TEXAS.

BRIEF

asserting unconstitutionality of paragraphs (5) and
(6) et seq. of Section 15a, Interstate
Commerce Act.

Statement.

By leave of Court, the undersigned attorneys and
counsellors of this Court, as *amici curiæ*, submit this
brief asserting the unconstitutionality of the statutory

provisions involved in the above-entitled suit, in the hope that the same may be of assistance in the decision of the important question before this Court. The undersigned are General Counsel, respectively, of the following companies: Southern Pacific Company; Lehigh Valley Railroad Company; Western Pacific Railroad Corporation; New York Central Railroad Company; Union Pacific Railroad Company; Chesapeake & Ohio Railway Company; Western Maryland Railway Company; Illinois Central Railroad Company; Delaware, Lackawanna & Western Railroad Company; Virginian Railway Company; Duluth, Missabe & Northern Railway Company; Chicago & Eastern Illinois Railway Company; Kansas City Southern Railway Company; El Paso & Southwestern Railroad Company; St. Louis Southwestern Railway Company and Wabash Railway Company; and Pere Marquette Railway Company; Assistant General Counsel of The New York, Chicago and St. Louis Railroad Company; and General Attorney of the New Orleans, Texas & Mexico Railway Company. The statute involved in this suit is of general application to railroad companies engaged in interstate commerce, and its provisions, if held valid, may in future operation substantially affect the interests of the above-named companies.

The Dayton-Goose Creek Railway Company brought the above-entitled suit in the District Court of the United States, for the Eastern District of Texas, seek-

ing to enjoin the enforcement of the provisions of paragraphs (5) and (6) *et seq.* of Section 15*a* of the Interstate Commerce Act (added by Section 422 of the Transportation Act, 1920) for the appropriation by the Government from railroad carriers engaged in interstate commerce of one-half of their net railway operating income in excess of 6 per cent. on the value of their transportation property, and for the restriction of the carriers' use of the remaining half. The District Court [Honorable R. W. Walker, United States Circuit Judge, Honorable Alex C. King, United States Circuit Judge, and Honorable Rufus E. Foster, United States District Judge sitting] denied an application for an interlocutory injunction and, on motion of the Government, dismissed the bill of complaint. From that action of the District Court the plaintiff has appealed to this court.

The text of Section 15*a* of the Interstate Commerce Act, added by Section 422 of the Transportation Act, 1920, approved February 28, 1920 [41 Statutes-at-Large, 488], is printed as an appendix to this brief.

POINT I.

The provisions of the statute appropriating a part of the net railway operating income, and restricting the use of a further part, are not a regulation of interstate commerce, but a direct confiscation of carriers' property and invasion of their property rights in violation of the Fifth Amendment.

The railroad situation confronting Congress as the occasion for the enactment of the Transportation Act is outlined in the opinion of this Court in *Wisconsin Railroad Commission v. Chicago, Burlington & Quincy Railroad Company*, 257 U. S. 563, at pages 582 to 584. In a word, the carriers were about to be released from the Federal war control, with their credit crippled by causes which had existed prior to Federal control, and which had prevented the development of the railroad facilities of the country proportionately with the country's growth, and in addition burdened with enormously increased operating expenses. It was deemed essential to provide a new policy for the regulation of carriers.

In the Senate Committee Report on the bill which resulted in the Transportation Act (Report No. 304 of the 1st Session, 66th Congress, on Senate Bill 3288, Calendar No. 231), the situation was stated, in part, as follows:

"In considering this phase of the subject, it should
"be constantly borne in mind that if our policy is to be
"private operation of the instrumentalities of transpor-

"tation there must be a large and constant inflow of
 "capital. As commerce increases in volume, the fa-
 "cilities of transportation must increase; and, without
 "reckoning the funds which must be secured to dis-
 "charge maturing obligations already in existence, it
 "will be conceded by everybody that immense sums will
 "be required from year to year for new construction,
 "additional equipment, and necessary improvement.
 "The capital thus demanded must be drawn from those
 "who have money to invest, and, of course, it must be
 "voluntarily contributed. If the people who have
 "money will not invest it in the transportation enter-
 "prise, private ownership and operation under public
 "control must necessarily fail. It is apparent, there-
 "fore, that any legislation which may be proposed upon
 "the hypothesis of private ownership and operation
 "must tender to the future investor reasonable security
 "for the investment he is asked to make and reasonable
 "assurance of such yearly return upon his money as
 "will induce him to enter the field. The better the secu-
 "rity and the more certain the return, the less will be
 "the rate required to attract the investment."

In the *New England Divisions Case*, 261 U. S. 184,
 this Court referred to the Transportation Act, 1920,
 as introducing into federal legislation a new railroad
 policy and said: "Theretofore, the effort of Congress
 "had been directed mainly to the prevention of abuses;
 "particularly those arising from excessive or discrim-
 "inatory rates. The 1920 Act sought to insure, also,
 "adequate transportation service. That such was its

"purpose, Congress did not leave to inference. The "new purpose was expressed in unequivocal language. "And to attain it, new rights, new obligations, new machinery, were created. The new provisions took a "wide range. Prominent among them are those specially designed to secure a fair return on capital devoted to the transportation service."

The provisions adopted to accomplish the purpose stated in the above quoted Committee Report and the *New England Divisions Case*, namely, to secure a return, to the railroads generally, calculated to attract new capital and to ensure an adequate transportation service, were those embodied in paragraphs (2), (3) and (4) of Section 15a. By these provisions the Commission is directed, in the exercise of its power to prescribe just and reasonable rates, to initiate, modify, establish or adjust rates so that the carriers in each rate group will earn an aggregate annual net railway operating income equal, as nearly as may be, to a fair return on the aggregate value of the railway property in such group used in the transportation service. The percentage constituting a fair return is fixed by the Act at 5½ per cent. for the first two years, with a possible allowance in the Commission's discretion of an additional one-half of one per cent. to provide for improvements chargeable to capital account, and after the expiration of the first two years the percentage is to be fixed by the Commission. In determining such percentage the Commission is directed to give due consideration to the transportation needs of the country

and the necessity of enlarging the transportation facilities in order to provide the country with adequate transportation.

The essential features of these provisions are a direction to make rates *on the group basis* and a mandate that the rates so made shall produce as nearly as practicable an *aggregate return for the group equal to a percentage of the aggregate property value of the group fixed*, by Congress first, and later by the Commission, *as a fair return*.

Paragraphs (2), (3) and (4) of Section 15a undoubtedly constitute a regulation of commerce. We do not question that their object—the promotion of the commerce of the whole country through the rehabilitation of the credit of the carriers and the necessary enlargement of transportation facilities—was within the granted power to regulate interstate commerce. We do not question that these provisions were appropriate and legitimate means to accomplish that object, subject to the qualification that the percentage constituting a fair return could not be conclusively fixed by Congress or the Commission. *Chicago, Milwaukee & St. Paul Ry. Co. v. Tompkins*, 176 U. S. 167, 173; *Lincoln Gas Co. v. Lincoln*, 250 U. S. 256, 267; *Bluefield Water Works and Improvement Co. v. Public Service Commission*, decided by this Court June 11, 1923.

Our challenge is directed to the subsequent provisions of Section 15a, those embodied in paragraphs (5) and (6) *et seq.* of that section.

Paragraph (5) is in the nature of an introduction to the substantial provisions of the subsequent sections.

It recites that it is impossible to establish uniform rates upon competitive traffic which will adequately sustain all the carriers without enabling some of such carriers to receive a net railway operating income substantially and unreasonably in excess of a fair return, and then declares that any carrier which receives a return so in excess of a fair return shall hold a part of such excess, prescribed in the succeeding paragraph, "as trustee for" the United States. Paragraph (6) provides that a carrier receiving in any year net railway operating income in excess of 6 per cent. on its property value shall place one-half of such excess in a reserve fund to be maintained by it and pay over the remaining half of such excess to the Interstate Commerce Commission for the purpose of establishing and maintaining a "general railroad contingent fund". Paragraphs (7) to (16) consist of regulations as to the reserve fund and the general railroad contingent fund.

For the sake of brevity, the provisions of paragraphs (5) to (16) will be collectively referred to as the income-appropriation provisions.

(a) It was the avowed purpose of the income-appropriation provisions to regulate the railway operating income of carriers, not by a regulation of their rates, but by taking from them a portion of their income, arbitrarily declared by the Act to be excessive.

The Senate Committee Report, *supra*, stated that during the pre-war test period the average net railway operating income of all the Class I railroads was 5.2 per cent. upon their aggregate property investment

and gave the returns realized by a number of individual roads during the same period, of which examples the highest rate of return was 7.54 per cent. and the lowest 1.77 per cent. Said report then states: "It is obvious that if the law gives to the carriers the assurance of income heretofore mentioned there should be a maximum beyond which an individual carrier shall not be permitted to retain for its own use all it may receive under a given body of rates. Referring to the illustrations already given, it is seen that with uniform rates, and they must be uniform in competitive territories, one carrier will receive an operating income of 2 per cent., another 4 per cent., another 6 per cent., another 8 per cent., and others still more. The bill fixes a standard of excess income and requires the carriers which receive an excess income (which will hereafter be explained in detail) to pay the excess to the transportation board for uses that have been mentioned and which will be more fully stated in a subsequent paragraph of this report". * * * " * * *

"If the lawyers who insist that taking excess income is unconstitutional are right in their premises, their conclusion would be unassailable. They assume that all the earnings of a given railway under a prescribed body of rates become the absolute property of the carrier which receives them. This is not true under the system which the bill creates; and, therefore, the conclusion is unsound. If there were but one railway in the country, it would be entirely possible for the regulating commission to fix rates for it under which it

"could not earn more than 6 or 7 per cent. upon the
 "value of its property, but we have a thousand railways;
 "and rates for transportation must be fixed with refer-
 "ence to all of them and to the needs of the people to
 "whom all of them render their service. These condi-
 "tions make it utterly impossible to fix rates which are
 "reasonable for one carrier, considered apart from all
 "the remainder. It is, therefore, in the competence of
 "Congress to declare that the income which any partic-
 "ular carrier receives beyond a fair return upon the
 "value of its property, it receives as a trustee for the
 "public and not as its own absolute property. If this
 "analysis of the power of regulation is not sustained,
 "then the authority granted in the Constitution is a
 "mere delusion."

The theory of the Committee is expressed in un-
 equivocal language. There is no pretence that the
 desired suppression of excess incomes is accomplished
 by rate regulation. On the contrary, it is stated that it
 is "utterly impossible to fix rates which are reasonable
 "for one carrier considered apart from all the re-
 "mainder." It is frankly recognized that the amount
 of alleged "excess income" seized will have been earned
 by the carrier from the prescribed body of rates. It is
 merely declared to be "obvious" that in consideration of
 the supposed greater assurance of a fair return, there
 should be a maximum beyond which an individual car-
 rier "shall not be permitted to retain for its own use all
 "it may receive". There is no claim that the portion of

income labelled "excess income" is differentiated from the income which the carrier is permitted to retain, by the manner of its acquisition or in any respect, except by the label given it by the statute because of its amount. The whole theory rests squarely upon the proposition that Congress can fix "a standard of excess income" and can prevent income realized in excess of that standard from becoming the carrier's absolute property by a declaration that such portion of its income is received by it "as trustee".

But we do not need to go outside the language of the Act itself to establish its purpose, for the recital in paragraph (5) makes the purpose entirely clear. This recital states:

"Inasmuch as it is impossible (without regulation and control in the interest of the commerce of the United States considered as a whole) to establish uniform rates upon competitive traffic which will adequately sustain all the carriers * * * without enabling some of such carriers to receive a net railway operating income substantially and unreasonably in excess of a fair return * * * it is hereby declared that any carrier which receives such an income so in excess of a fair return, shall hold such part of the excess, as hereinafter prescribed, as trustee for, and shall pay it to, the United States".

In the statute, as in the committee report, the impossibility of limiting the income by making rates for the individual carrier is recognized. The statute like

the report, frankly recognizes all the income, whether within or beyond the limit of a "fair return", as received from the railroad operations under prescribed rates, without differentiation of character. The declaration of a trust character, asserted by the committee report to be competent and controlling, is made, and it is attempted to give this declaration the appearance of a regulation of commerce by the parenthetical phrase in the above quotation.

(b) Net income realized from operations in interstate commerce is not a part of commerce and the power to regulate interstate commerce does not include the regulation of such net income.

In *Second Employers' Liability Cases*, 223 U. S. 1, this Court said, at page 48: "As is well said in the brief 'prepared by the late Solicitor General: 'Interstate commerce—if not always, at any rate when the commerce 'is transportation—is an act. Congress, of course, 'can do anything which, in the exercise by itself of a 'fair discretion, may be deemed appropriate to save 'the act of interstate commerce from prevention or interruption, or to make that act more secure, more 'reliable or more efficient' ". In the same case it was said, at page 47: "This power over commerce among the 'States, so conferred upon Congress, is complete in 'itself, extends incidentally to every instrument and 'agent by which such commerce is carried on, may be 'exerted to its utmost extent over every part of such 'commerce, and is subject to no limitations save such

"as are prescribed in the Constitution. But, of course, "it does not extend to any matter or thing which does "not have a real or substantial relation to some part of "such commerce."

In the *First Employers' Liability Cases*, 207 U. S. 463, the Court said, at page 502: "It remains only to "consider the contention which we have previously "quoted, that the act is constitutional, although it em- "braces subjects not within the power of Congress to "regulate commerce, because one who engages in inter- "state commerce thereby submits all his business con- "cerns to the regulating power of Congress. To state "the proposition is to refute it." The act then under consideration attempted to regulate the liability of every common carrier engaged in interstate commerce for personal injuries suffered by its employes without qualification or restriction as to whether the employes at the time of their injury were engaged in interstate commerce or in intrastate commerce. Therefore, in accordance with the holding in the quotation last above that one who engages in interstate commerce does not thereby submit all his business concerns to the regulating power of Congress, the court held that act unconstitutional as extending to a subject not within the regulating power of Congress.

A number of other decisions of this Court have established limitations upon the subjects which Congress may regulate under the power to regulate commerce, comprehensive as is that power. Thus in *Ham-*

mer v. Dagenhart, 247 U. S. 251, it was held that an act, although adopted under the guise of a regulation of commerce in that it prohibited the movement in interstate commerce of the products of child labor, transcended the authority delegated to Congress over commerce. It was held that the *production* of articles intended for shipment in interstate commerce is not a part of such commerce but a matter of local regulation. It was said, at page 272: "The making of goods "and the mining of coal are not commerce, nor does the "fact that these things are to be afterwards shipped or "used in interstate commerce, make their production a "part thereof." In *Delaware, Lackawanna & Western R. R. Co. v. Yurkonis*, 238 U. S. 439, it was held that the mining of coal by a railroad company, although for use in its locomotives in the conduct of interstate commerce, did not constitute interstate commerce. See also *United Mine Workers v. Coronado Co.*, 259 U. S. 344, 407-8. Again in *Adair v. U. S.*, 208 U. S. 161, it was held that a federal statute making it a criminal offence for an interstate carrier to discharge an employe because of his membership in a labor union was repugnant to the Fifth Amendment as not embraced by the power of Congress to regulate interstate commerce and the Court said, at page 178: "Such "relation to a labor organization cannot have, *in itself* "and in the eye of the law, any bearing upon the commerce with which the employe is connected by his "labors and services".

Applying the principle of the few cases cited under

this heading, it would be concluded, even in the absence of a precise precedent, that the limitation of net income resulting from operations in interstate commerce is not comprehended by the power to regulate such commerce. Commerce is an act. The net income resulting from the performance of that act is the fruit of the act but not a part of the act itself. The net income realized from the performance of the act of interstate commerce is a matter subsequent to and distinct from the commerce, as fully as the manufacture of goods to be shipped in interstate commerce and the mining of coal to be similarly shipped or to be used in the performance of interstate commerce are matters prior to and distinct from the commerce itself. But precise authority supporting this conclusion is not wanting.

In *United States Glue Co. v. Town of Oak Creek*, 247 U. S. 321, there was involved an income tax levied under a Wisconsin law. The taxpayer contended that a portion of the tax having been imposed upon income derived from interstate commerce was void as a burden upon such commerce. The income so in question was derived in part (1) from goods sold to customers outside of Wisconsin and delivered from the taxpayer's factory in Wisconsin and in part (2) from goods sold to customers outside of the state, the contracts of sale and the deliveries being made by branch offices of the taxpayer in other states and only the manufacture of the goods, prior to their sale, having occurred in Wisconsin. Notwithstanding the well-established principle that a state

tax upon gross receipts from interstate commerce is void as a burden upon such commerce (for example, *Philadelphia S. S. Co. v. Pennsylvania*, 122 U. S. 326), it was held that the Wisconsin income tax law was not objectionable. It was pointed out that such a tax levied upon net income affected the revenues from interstate commerce in no greater degree than local taxes imposed upon property and franchises employed in interstate commerce, the validity of which had long been established, since both classes of taxes must be paid from the net returns of the business and diminish such returns in the same sense. The Court said, at page 328:

"The difference in effect between a tax measured by gross receipts and one measured by net income, recognized by our decisions, is manifest and substantial, and it affords a convenient and workable basis of distinction between a direct and immediate burden upon the business affected and a charge that is only indirect and incidental. A tax upon gross receipts affects each transaction in proportion to its magnitude and irrespective of whether it is profitable or otherwise. Conceivably it may be sufficient to make the difference between profit and loss, or to so diminish the profit as to impede or discourage the conduct of the commerce. A tax upon the net profits has not the same deterrent effect, since it does not arise at all unless a gain is shown over and above expenses and losses, and the tax cannot be heavy unless the profits are large".

Peck v. Lowe, 247 U. S. 165, involved the question whether the federal income tax, so far as levied upon net income derived from an exporting business, was contrary to the constitutional prohibition against the levy of taxes or duties on exports. While recognizing that previous decisions had interpreted the prohibition in question as requiring that exportation must be free from any tax which directly burdens such exportation, such as taxes upon charter parties, upon export bills of lading, upon policies of marine insurance, this Court held that neither the letter nor the spirit of that constitutional prohibition excluded a tax upon net income derived from the exportation business. The Court said, at page 175: "At most, exportation is affected only indirectly and remotely. The tax is levied after exportation is completed, after all expenses are paid and losses adjusted, and after the recipient of the income is free to use it as he chooses. Thus what is taxed—the net income—is as far removed from exportation as are articles intended for export before the exportation begins".

The two cases above cited are precisely in point and conclusive upon the proposition now under discussion. Congress may of course, through the regulation of their rates, legitimately regulate and limit the operating *revenues* of interstate carriers. This was the power exercised and upheld in the *New England Divisions Case*, *supra*. But the income-appropriation provisions are not and do not purport to be

a regulation of rates. Such control over the operating *revenues* of interstate carriers belongs exclusively to the federal authority. The states may not control such revenues in any way. But the *net income*, determined by the charging of expenses and losses to the operating revenues, is a different matter. It is removed at least another degree from the act of transportation and is too far removed from the act of transportation or interstate commerce to constitute a part or an incident thereof. The cases cited, recognizing the power of the states to tax such net income derived from interstate operation definitely establish the distinction. It is, therefore, beyond the commerce power to regulate such net income.

(c) The net income which is the subject of the income-appropriation provisions is the unqualified property of the carriers, and evidences elements of value inherent in their railroads. A taking of the income is a confiscation not only of the amount in money so taken but also of a part of the value of the railroads themselves.

That the net income of the carriers is their property might well be rested upon the cases cited under the last preceding subpoint. To repeat a part of the language used in *Peck v. Lowe, supra*, "The tax is "levied after exportation is completed, after all expenses are paid and losses adjusted, and after the "recipient of the income is free to use it as he chooses." Like the tax there in question, the income-appropriation provisions of Section 15a operate after the interstate

transportation is completed, after all expenses are paid and losses adjusted, and, therefore, in the language of *Peck v. Lowe*: "after the recipient of the income is "free to use it as he chooses."

1. *The net income is earned from rates which must be presumed to be reasonable, and so is absolute property.*

The rates under which the net operating railway income are derived must be either unjust and unreasonable or just and reasonable rates. A carrier has no right to retain collections of transportation charges which are unreasonable. But any effort to sustain the income-appropriation provisions of this law on the theory that the subject-matter of the appropriation is the proceeds of unjust and unreasonable rates encounters insurmountable obstacles which are dealt with under Point II of this brief. If the rates are just and reasonable, the carrier is entitled to the receipts therefrom as its property, and the taking of any part of such receipts (except under a valid tax) equally with the taking of any other property of the carrier is prohibited by the Fifth Amendment.

We submit that it must be conclusively assumed, for the purposes of this case, that the rates from which the net railway operating income sought to be appropriated were derived were just and reasonable, subject to the power of the Commission reserved by paragraph (2) of Section 15a to find that particular rates are unjust or unreasonable.

Up to the enactment of the original Act to regulate commerce the charges of common carriers were governed in this country as they had long been in England by the rule of the common law that rates must be just and reasonable. *Interstate Commerce Commission v. Baltimore & Ohio R. R. Co.*, 145 U. S. 263, 275. The original Act to regulate commerce of 1887 prescribed the same rule and was merely declaratory of the common law, *Maximum Rate Case*, 167 U. S. 479, 501. That rule is still expressed in Section 1 of the Interstate Commerce Act as it exists today. Paragraph (2) of Section 15a recognizes the standard of justness and reasonableness as the basic rule of rate-making under the present law, for it is expressed that the group basis rule of rate-making laid down for the Commission's guidance is to be observed "in the exercise of the Commission's power to prescribe just and reasonable rates". The new rule of rate-making subtracts nothing from the former rights of the carriers to just and reasonable rates. If any change has been effected by the new rule, there has been something added by the affirmative recognition and declaration that the rates which it is just and reasonable for the shipper to pay are rates sufficient to provide for the enlargement of transportation facilities commensurate with the growth of the country's need for transportation.

The Interstate Commerce Commission is the sole arbiter of the justness and reasonableness of interstate rates. *Texas & Pacific Ry. Co. v. Abilene Cotton Oil Co.*, 204 U. S. 426. This has not been changed by any

provision of the Transportation Act. Pursuant to the authority of paragraph (2) of Section 15a, the Commission in August, 1920, prescribed general rate increases for the various rate groups in *Ex Parte 74, Increased Rates, 1920*, 58 I. C. C. 220. The rates so prescribed are the rates from which the net railway operating income involved in the present case were derived, as far as it came from interstate business. Said rates constituted the lawful rates for the use of every carrier of the group for which they were prescribed. There attaches to them as complete and conclusive sanction as to reasonableness as if they had been specifically named in an act of Congress. Their character of finality is emphasized by the proviso to paragraph (2) which allows the Commission "reasonable latitude" to modify and adjust particular rates. The body of rates so prescribed under paragraph (2) must necessarily be reasonable, judged as a whole, for the average carrier of the group—average as to earning capacity, operating costs and property value—for this is in effect the premise of the rate structure of the group. If the rates are reasonable for the public to pay for the services of the average carrier or the less-than-average carrier of the group, they must be reasonable as charges for the services of the more prosperous carrier also.

It has never been held that the boundary line of confiscation, say a 6 per cent. return, is the maximum a carrier may lawfully and properly earn and retain under rates just and reasonable to the public. The use of a

specified percentage of return on property value, usually but not always 6 per cent., has always been limited to the function of determining whether an entire body of rates prescribed under governmental authority is so low as to amount to the use (the taking) of the carriers' property by the public without compensation. In the language of *Smythe v. Ames*, 169 U. S. 466, 546, the judicial question in this class of cases is "whether the Legislature has, under the guise of regulating rates, exceeded its constitutional authority, and "practically deprived the owner of property without due "process of law". See also *Railroad Commission Cases*, 116 U. S. 307, 331; *Wilcox v. Consolidated Gas Co.*, 212 U. S. 19, 41; *Reagan v. The Farmers' Loan and Trust Co.*, 154 U. S. 362, 397, 410.

The fact that one or more carriers out of a larger number in a given territory may realize a greater profit than the average or less-than-average carriers in that territory out of the rates legally established for that group in no sense involves an extortion or overcharge. There is nothing morally or legally wrong in a carrier realizing a large net profit from a schedule of reasonable rates. The fact that the situation and position of the carrier is such that it can show a large profit upon a schedule of rates which the Commission finds it proper to establish for all the carriers in the same territory evidences the exceptional value of the fortunate line and/or the greater efficiency of its operations.

From the same schedule of rates, just and reasonable to the carriers and to the public, different results

will be obtained by different carriers in the same general territory or competing for the same business. The reasons and causes contributing to the difference in operating results cannot be comprehensively catalogued. They are partly results of fortunate location and other natural advantages, and partly the results of foresight and wisdom in management and efficiency of operation.

So long as the rates from which the earnings are derived are just and reasonable, the relatively greater income of one carrier, to whatever cause due, is its absolute property, as fully as the smaller income of some other carrier is its absolute property.

It is the intent of the income-appropriation provisions under consideration to annul all advantages of the more successful carriers, whether due to location and other natural causes, or to superior management and operation. It is pertinent to quote from the opinion of the Commission in *Investigation and Suspension Docket No. 26*, 22 I. C. C. 604, at page 625: "A further consideration which moves us to permit these advanced rates is that we regard it as unfair to take from the carrier whatever of profit it may secure by reason of improvement in its plant and adoption of the most modern methods. If our railroad systems are to remain in private hands, stimulus must be given to the initiative and imagination of railroad operators. * * * This road is one of the most prosperous in the country, and it is largely so because of the enterprise of its officials in developing a great business and in handling it in the most economic method".

2. The net income evidences elements of value which are an essential part of the railroad property.

While greater efficiency in conducting operations and in soliciting traffic may be one of the causes contributing to the greater net income realized by one carrier as compared with another, the difference in net income is more often and to the greater extent due to superior location. Such superior location may be an accidental advantage or it may be due to sound judgment exercised in the original location of the road, to a long-practiced and intelligent policy in encouraging and assisting in the development of the country, and to a generous and wise expenditure of additional capital in improving and enlarging its facilities. In any event, it is an element of value.

The railroad business is essentially a competitive business. It operates in a competitive field under a reasonable rate schedule fixed for all of the roads in that territory. It is an axiom of economics that where competitive forces act freely, value is the result of the forces of supply and demand. The true value of a railroad depends primarily upon the demand for its transportation service, the extent to which in competition with its rivals it can supply that service, and the economy with which it can do it.

The same rates must be fixed for the entire territory. Under a schedule of rates thus fixed, it will always occur that certain roads will be able to handle

more traffic and at a greater profit than others, and there will inevitably emerge certain differentials of value because of the possession by certain roads of certain qualities and potentialities which are the very crux of the question of their economic value. These differentials will be indicated by differences in earnings, which are the evidences of the existence of certain elements of value. The earnings themselves are not the cause, but the effect, of value arising from qualities inherent in the property. These are qualities resulting largely from location. They exist because of factors dependent on location such as the density of population, the number and diversity of industries, the productivity of the territory served, the relationship of the carrier's line to centers of population and industry, and the location of the carrier's terminals in cities. Factors of that sort affect the demand for the carrier's facilities and the economy and efficiency with which the demand can be served. Certain of the factors of location are reflected in the degree of the efficiency and economy of operation, such as the relative directness of the carrier's route, the gradients, the amount of curvature, and a great variety of physical conditions and qualities arising from the nature of the country traversed, and its topographic, climatic, and other conditions. These qualities and factors are numerous and complex. They are incidents of rights in private property. They are qualities of the property, decisive of its value.

Such elements of value are reflected in superior earning capacity. They are like the elements of value in the location of a business lot. Assume that two men purchase business lots for the same price on different streets of the same city and that business development greatly increases the utility of one of these lots and its economic value, but not of the other. That increase belongs to the owner. It is clear that any statute which would deprive the owner of the better lot of the increased revenue due to its superior location, thereby virtually making it equivalent in value to the poorer lot, would destroy that differential increment in value due to the advantage of location. Such an appropriation would violate established conceptions of rights in private property. By an exact parity of reasoning, a confiscation of the value of the property is effected when an appropriation is made of the income, realized under a competitive rate schedule fixed as reasonable for a group of carriers, of a road which develops a superior degree of utility and economy because of physical and other qualities of its property, due to its location, as, for example, a superior route secured in pioneer days when it avoided grades and tunnels, its location with reference to centers of population, and trade routes, and its efficiencies in construction and operation. The effect of the income-appropriation provisions is to confiscate these superior elements of location and elements of value.

Such appropriation of elements of value due to location would not be sanctioned were it attempted in the

case of city building sites or farm property. The appropriation cannot be justified in the case of railroad property, unless it is held that railroad property is not within the category of private property. But railroad property is private property. The attempt has been made to prevent the public utility from securing a return on elements of value in the category of the so-called "unearned increment", but thus far such attempts have failed because it has been held that the property of a public utility is private property and that such elements, therefore, are not subject to confiscation.

In the *Minnesota Rate Cases*, 230 U. S. 352, it was argued that a railroad is not private property, and it was urged that elements of value in railroad property partaking of the nature of the value inherent in other private property were not protected by the Constitution. But this Court repudiated the contention, saying at page 433:

"The property of the railroad corporation has been devoted to a public use. There is always the obligation springing from the nature of the business in which it is engaged—which private exigency may not be permitted to ignore—that there shall not be an exorbitant charge for the service rendered. But the State has not seen fit to undertake the service itself; and the private property embarked in it is not placed at the mercy of legislative caprice. It rests secure under the constitutional protection which extends not merely to the title but to the right to receive just compensation for the service given to the public."

And further, at page 454:

"The property is held in private ownership and it "is that property, and not the original cost of it, of "which the owner may not be deprived without due "process of law."

See also: *San Diego Land and Town Co. v. National City*, 174 U. S. 739; *Wilcox v. Consolidated Gas Company*, 212 U. S. 19; *San Joaquin Company v. Stanislaus County*, 233 U. S. 454.

To hold that the income-appropriation provisions are valid would, therefore, sanction the confiscation, by this method, of elements of value, which this Court has consistently refused to sanction in the rate-confiscation and condemnation cases. Such a holding would foreclose for the future the reliance upon the value of the property as a test of Constitutional protection, because the confiscation of income, which is in effect an appropriation of the superior elements of location reflected only in income, is necessarily a confiscation of those essential elements of value and a destruction of the value of the property due to them.

(d) The statutory declarations that the income to be appropriated is excess income and that it is held in trust are not competent to qualify the title of the carriers thereto.

The declarations in this statute that the net railway operating income sought to be appropriated is "in excess of a fair return" and that the carrier holds it "as trustee for" the United States are ineffective to deprive such income of its character as the absolute

property of the carrier. Nor is the perfunctory attempt by the parenthetical language of the recital of paragraph (5) to characterize these provisions as a regulation of commerce effective to make that a regulation of commerce which in fact is a plain excess of the power over interstate commerce. These terms are mere euphemisms to soften or disguise the purpose of confiscation. They cannot overcome the stubborn facts.

In *Galveston, Harrisburg & San Antonio Ry. Co. v. Texas*, 210 U. S. 217, it was said, at page 227: "Neither the state courts nor the legislatures, by giving the tax a particular name or by the use of some form of words, can take away our duty to consider its nature and effect".

In *Chicago, Burlington & Quincy R. R. Co. v. Drainage Commissioners*, 200 U. S. 561, it was said, at page 593: "If the means employed have no real, substantial relation to public objects which the government may legally accomplish; if they are arbitrary and unreasonable, beyond the necessities of the case, the judiciary will disregard mere forms and interfere for the protection of rights injuriously affected by such illegal action."

In *Hammer v. Dagenhart*, 247 U. S. 251, and in the *Child Labor Tax Case*, 259 U. S. 20, the statutes involved were held invalid because their purpose was to regulate the employment of child labor, a matter beyond the federal power, although the statutes were enacted, in the one case in the form of a regulation of commerce, and in the other in the form of a tax law.

In *Adair v. U. S.*, 208 U. S. 161, the statute was held invalid because its real subject-matter was the membership of employees in labor organizations, although it was enacted under the guise of a regulation of interstate commerce. In *Norwood v. Baker*, 172 U. S. 269, it was held that property was taken without due process although the proceeding was in form taxation. Citations to the same effect might be multiplied indefinitely.

We believe we have demonstrated that the net railway operating income of interstate carriers is not a part or incident of interstate commerce and is at least one degree removed from the power to regulate such commerce. The power of Congress to affect such income in any way must be exerted and will be exhausted before the net railway operating income is realized and ascertained. That power is confined to action upon the act of commerce itself or the incidents of commerce which may be deemed a part of it, of which the transportation rates are the principal but not the sole example. But in the case of the income-appropriation provisions under consideration no attempt has been made to affect the amount of the net railway operating income through such legitimate means. Instead, Congress has resorted to a succession of legislative fiats, namely: (1) that a fair return for a group of carriers is $5\frac{1}{2}$ per cent. for the first two years, and thereafter whatever the Commission shall in its judgment determine; (2) that one-half of any net railway operating income in excess of 6 per cent. is "substantially and unreasonably in excess of a fair return", and

(3) that such alleged substantial and unreasonable excess is held "in trust for" the United States. Not one of these three legislative declarations is it competent for Congress to make. The amount which constitutes due compensation for a taking of property or a fair return for the use of property in public service is a judicial and not a legislative question. *Chicago, Milwaukee & St. Paul Ry. Co. v. Tompkins*, 176 U. S. 167. *Lincoln Gas Company v. Lincoln*, 250 U. S. 256. *Monongahela Navigation Co. v. United States*, 148 U. S. 312, 327. *Seaboard Air Line v. United States*, 261 U. S. 299, 304. The declarations that a part of the net railway operating income is substantially and unreasonably excessive and that it is held in trust amount to an attempt to create a trust solely by the declaration of the beneficiary without the consent of the owner of the property which is to be appropriated as the trust fund. There is no corpus of the trust. No funds are segregated or identified as funds held for the Government. The "trust" would be imposed upon a wholly unidentified portion of the carrier's general assets used by it in its business.

Of course, the theory of these provisions was that a statutory declaration that net railway operating income realized in future operations in excess of a specified amount should not become the property of the carrier would arrest the vesting of title to the operating revenues and hold it in suspense until the whole operations of the year were completed and the net railway operating income of the year determined. The theory

is utterly untenable. The act makes no provision for anything which affects the character of the revenues as they accrue, or which can have the effect of arresting the vesting of absolute title. The carrier from whom this income appropriation is to be made is left to operate under the rates prescribed by the Commission, the rates applicable to all carriers. There is no declaration that such rates will be deemed unreasonable in the case of any carrier. There is no provision for an adjudication by the Commission that such body of rates is unreasonable as to any carrier. There is simply an appropriation at the end of the year of a part of the carrier's net railway operating income, and the amount so appropriated is in no way identifiable with any particular shipment or class of traffic and is not even capable of identification as the product of interstate business as distinguished from intrastate business.

The regulation of commerce is essentially prospective in its operation. The income-appropriation provisions, however, are essentially an attempt to regulate by *ex post facto* procedure. The proponents of this legislation would, of course, not claim that Congress could enact a law appropriating a specified part of the income realized by interstate carriers from operations of a year or years prior to such enactment. This would admittedly be a plain case of confiscation. But the only difference between such enactment and the statutory provisions under consideration is that in the supposed case no warning of the intended confiscation was given the victims while in the present case they

have been warned. *The statutory declarations that a part of the income is unreasonably in excess of a fair return and that the same is held in trust for the United States amount to nothing more than a warning or notice of the contemplated confiscation.* We submit that judicial sanction cannot be given to the theory that a taking of property can be legalized simply by giving notice or warning that if the citizen owns described property at a specified date in the future it will be taken from him.

(e) This attempted appropriation of income is not an indirect or consequential result of any legitimate exercise of Congressional power, but is a direct confiscation of property.

Congress may adopt means to accomplish an object within its granted powers, although such means incidentally and consequentially affect private property, without thereby infringing the rights of property guaranteed by the Fifth Amendment,—the damage is *damnum absque injuria*. *Gibson v. U. S.*, 166 U. S. 269, 275; *Transportation Co. v. Chicago*, 99 U. S. 635; *Union Bridge Co. v. U. S.*, 204 U. S. 364, 388. But, even if the object sought to be accomplished by Congress is within its granted power, it does not justify the actual taking or direct invasion of private property *Bedford v. U. S.*, 192 U. S. 217, 225.

In *Monongahela Navigation Co. v. U. S.*, 148 U. S. 312, it was said at page 336:

“Congress has supreme control over the regulation of commerce, but if, in exercising that supreme control,

"it deems it necessary to take private property, then it
"must proceed subject to the limitations imposed by this
"Fifth Amendment, and can take only on payment of
"just compensation. The power to regulate commerce
"is not given in any broader terms than that to establish
"post-offices and post roads; but, if Congress wishes to
"take private property upon which to build a post-office,
"it must either agree upon the price with the owner, or
"in condemnation pay just compensation therefor."

In *Chicago, Burlington & Quincy v. Drainage Commissioners*, 200 U. S. 561, the court said at page 593:

"If in the execution of any power, no matter what it
"is, the Government, Federal or State, finds it necessary
"to take private property for public use, it must obey the
"constitutional injunction to make or secure just com-
"pensation to the owner."

We have already shown that the purpose primarily sought to be accomplished by the provisions of Section 15a was to rehabilitate the credit of the carriers and to provide rates adequate not only to sustain the carriers in their then existing condition, but to enable them to increase their facilities to meet the growing transportation needs of the entire country. To this end, the rule of rate-making embodied in paragraphs (2), (3) and (4) was adopted. This rule of rate-making on a group basis would presumably result in increased gross and net revenues to carriers in the group and individually. In any event it was the intention of Congress to sanction or encourage a more liberal rate policy than had been

practised in the past. The primary purpose was within the power of Congress and the rule of rate-making adopted as a means was appropriate to the purpose. But when this prescribed rule of rate-making should be put in force by the Commission and adequate revenues to rehabilitate the credit of the carriers should be derived therefrom, the primary purpose of Congress would be wholly accomplished. No further means were necessary to its attainment.

But it was feared that, as recited in paragraph (5), under the rate policy so prescribed, some carriers would derive an income "substantially and unreasonably" in excess of the percentage of value determined upon as constituting a fair return, or, in other words, that some carriers would earn more than it was contemplated and desired the average carriers should realize and therefore more than Congress was willing they should retain. If the result so feared should come to pass, the primary object for which Congress was working would be in no way defeated thereby. The fact that some carriers might earn more than the return contemplated for the average carriers, or even the fact that some carriers might earn an amount unreasonably in excess of a "fair return", would not tend in the least to defeat such primary object and purpose of the legislation. It might make a few carriers unnecessarily prosperous. It might incite criticism of the scale of rates by the public based on the favorable results to a few carriers and ignoring the fact that the rates were made with reference to the needs and deserts of the

average carriers and were just and reasonable by such standard. But any such public criticism, apprehended by Congress, while having possible political significance, would have no tendency to impair the adequacy of the revenues of the carriers as a whole, the rehabilitation of their credit and the proper development of the nation's transportation plant, all of which constituted the primary object of the legislation. Any such prosperity of a few carriers, and any such consequent public criticism *would be only a consequence and result of the rule of rate-making adopted* as an appropriate means of accomplishing the end sought by Congress. They would constitute a new situation and a separate and distinct problem. To avoid that consequence and result Congress has seen fit to provide for depriving the prosperous carriers of such amounts of their railway income as Congress has chosen to consider excessive (and to do so simply by the legislative declaration, made in advance, that such portion of income, if realized, shall be held in trust by the carrier), and for restrictions upon the carriers' use of a further portion of their income. This cannot be considered, by any stretch of the imagination, a means, either appropriate or inappropriate, adopted for the accomplishment of an object within the power to regulate commerce. Congress has by paragraphs (2) to (4) of Section 15a adopted an appropriate means, to wit, a rule of rate-making, for accomplishing the promotion of interstate commerce which was the primary object of its action. The provisions embodied in paragraphs (5) and (6), to wit,

the appropriation and control of the disposition of net railway operating income, do not constitute another means adopted to accomplish the primary purpose, but a means of nullifying a consequence and result, deemed undesirable, of the means adopted to attain the primary end. As such, these provisions have no relation, in the eye of the law, to any object within the power to regulate commerce, but constitute the taking of and interference with the property of the carriers, as the end and object, in the legal sense, of the action.

(f) The allocation of a part of the net railway operating income to a reserve fund and the restriction upon the use of such fund by the carrier amount in legal effect to a deprivation of property without due process, equally with the complete appropriation of a portion of the net railway operating income.

The direction of paragraph (6) of Section 15a is that one-half of the net railway operating income in excess of 6 per cent. on the property value "shall be placed in a reserve fund established and maintained by such carrier". Paragraph (7) provides that for the purpose of paying dividends or interest or rent for leased roads a carrier may draw upon this reserve fund but only to the extent that its net railway operating income in any year is less than 6 per cent. upon its property value. By the provisions of paragraph (8) the reserve fund need not be further added to after it aggregates a sum equal to 5 per cent. upon the carriers' property value and after this maximum has been at-

tained the one-half of the net railway operating income in excess of 6 per cent., theretofore required to be placed in the reserve fund, may be used by the carrier for any lawful purpose. But it should be observed, first, that the reserve fund never, even when the net railway operating income falls below 6 per cent., can be used for any purpose other than the payment of dividends, interest and rent for leased road. It cannot, for example, be appropriated for additions and betterments. It should be observed in the second place that, so long as the carrier continues to realize an excess of 6 per cent. of net railway operating income, the amount accumulated in the reserve fund cannot be used for any purpose whatever, but is perpetually impounded. Even after it has been accumulated to the prescribed maximum of 5 per cent. upon the entire property value it must be kept absolutely intact, unless, and then only to the extent that, the net in any year shall fall below the 6 per cent. standard.

It is established by the decisions of this court that the value of property results from the use to which it is put and depends upon the profitableness of that use, present and prospective, actual and anticipated. As stated in *Cleveland, Cincinnati, Chicago & St. Louis Ry. Co. v. Backus*, 154 U. S. 439 at 445: "There is no "pecuniary value outside of that which results from "such use." This language was quoted with approval in *Branson v. Bush*, 251 U. S. 182, 187.

In *Buchanan v. Warley*, 245 U. S. 60, the question concerned was the validity of a city ordinance adopted

for the expressed purpose of preventing conflict and ill feeling between the white and colored races and to preserve the public peace and to promote the general welfare, which made it unlawful for a person of either race to occupy a house upon any block upon which the greater number of houses were occupied by persons of the other race. The invalidity of the ordinance was asserted by a white person who had contracted to sell to a colored person a house which under the terms of such ordinance could not be occupied by a colored person. The ordinance was held invalid. The court said, at page 74: "Property is more than the mere thing which a person owns. It is elementary that it includes the right to acquire, use, and dispose of it. The Constitution protects these essential attributes of property. *Holden v. Hardy*, 169 U. S. 366, 391. Property consists of the free use, enjoyment, and disposal of a person's acquisitions without control or diminution save by the law of the land. 1 Blackstone's Commentaries [Cooley's Ed.], 127."

In *Coppage v. Kansas*, 236 U. S. 1, the court said, at page 18: "In short, an interference with the normal exercise of personal liberty and property rights is the primary object of the statute, and not an incident to the advancement of the general welfare. But, in our opinion, the Fourteenth Amendment debar[s] the States from striking down personal liberty or property rights, or materially restricting their normal exercise, excepting so far as may be incidentally necessary for the ac-

"complishment of some other and paramount object, and one that concerns the public welfare."

In *Great Northern Railway Co. v. Minnesota*, 238 U. S. 340, it was said, at page 346: "A railroad's possessions are subject to its public duty but beyond this and within charter limits, like other owners of private property, it may control its own affairs."

In *Oklahoma v. Kansas Natural Gas Co.*, 221 U. S. 229, a statute which prevented the removal of natural gas from the state of its production was held invalid. This Court said, at page 254: "It does not alone regulate the right of the reduction to possession of the gas, but when the right is exercised, when the gas becomes property, takes from it the attributes of property, the right to dispose of it; indeed, selects its market to reserve it for future purchasers and use within the State on the ground that the welfare of the State will thereby be subserved. The results of the contention repel its acceptance. Gas, when reduced to possession, is a commodity; it belongs to the owner of the land, and, when reduced to possession, is his individual property subject to sale by him, and may be a subject of intrastate commerce and interstate commerce."

The requirement that a part of the net railway operating income shall be set aside as a reserve fund and the limited use permitted of this reserve fund substantially impair the carrier's enjoyment of this portion of its funds. If, as heretofore argued, the net railway operating income accrues to the carrier as its property

and the attempted assertion of a trust does not operate to arrest the vesting of such title, the use of the fund represented by such net railway operating income is beyond the power of government dictation and restriction. A substantial restriction upon the use of the carrier's funds is as much a deprivation of its property right therein as is the actual and complete appropriation of such funds by the government.

(g) The income-appropriation provisions cannot be sustained on the theory that their result is equivalent to a result which might be obtained by prescribing different rates for different roads.

The argument has been advanced by advocates of this law that different rates may lawfully be prescribed for different carriers in the same territory, classified according to their prosperity, that by this means a limitation of the incomes of carriers to a selected rate of return could have been effected, and that the carriers have no ground for complaint against the statute under consideration which, it is said, merely accomplishes the same result by a different method. The foregoing argument appears to involve a premise of law, a premise of fact and a conclusion, each of which we believe to be unsound.

The premise of law is that different rates may lawfully be prescribed for different roads upon the sole consideration of their income and for the sole purpose of limiting their net income to a selected rate of return, provided only that the rates so prescribed shall not as to

any particular carrier so reduce its aggregate return as to amount to confiscation. It is true that it is not required, as a matter of law, that rates shall be the same for the same distance over two different roads (*Interstate Commerce Commission v. Union Pacific R. R. Co.*, 222 U. S. 541, 551), or that all turnpike companies in a state shall be placed upon an equality of rates (*Covington & Lexington Turnpike Road Company v. Sandford*, 164 U. S. 578, 598). But in the former of the cases just cited it was held merely that the Commission did not act arbitrarily in continuing a difference in rates which the carriers themselves had established and maintained, giving consideration to the weight and character of the reasons and causes which prompted and justified the carriers in their action; and in the latter case it was held merely that the circumstances of each turnpike company must determine the rates properly allowed for its use and that "all the circumstances" must be considered in determining what compensation for the use of the property will be just both to the turnpike company and to the public. Cases are cited in support of this legal premise involving state laws classifying railroads according to earnings, of which *Chicago, Burlington & Quincy R. R. Co. v. Iowa*, 94 U. S. 155, has been the leading citation. In that case the carrier attacked Chapter 68 of the 1874 laws of Iowa which classified railroads in three classes according to the amount of their gross earnings per mile and provided different maximum rates for each class. The principal contention made by the carrier was that under its char-

ter its rates could not be fixed by the state. The only reference by this Court to the matter of classification was as presenting the question whether the law was in conflict with the provision of the state constitution requiring all general laws to have a uniform operation. In *Chicago & Grand Trunk Railway Co. v. Wellman*, 143 U. S. 339, the only point decided or discussed was the refusal of the trial court to instruct the jury for the defendant, it being held that the evidence was too meagre to have justified such instruction. *Dow v. Beidelman*, 125 U. S. 68, involved an attack upon an Arkansas law prescribing maximum rates of 8 cents a mile on railroads 15 miles or less in length, 5 cents on roads over 15 and less than 75 miles, and 3 cents on roads over 75 miles in length. The case was dismissed because the Court considered the record insufficient to show that the return to the complainant under the three cent rate would amount to confiscation. A contention that the carrier had been denied the equal protection of the laws was dismissed with the statement [p. 691]: "The Legislature, in the exercise of its power of regulating fares and freight, may classify railroads according to the amount of the business which they have done or appear likely to do". The statement quoted falls far short of sustaining the legal premise of the argument under consideration. At most, it recognizes classification on the basis of earnings per mile as *not violating the equal protection clause*, for the purpose of imposing *some* differentiation in rates. It certainly does not sustain the proposition that rates may

be made upon the sole consideration of the prosperity of the carrier, or the proposition that they may be made for the sole purpose of limiting the carrier's income to a selected return, with due regard to the provisions of the Fifth Amendment. In further support of the said legal premise, reference has also been made to the confiscation cases in which an entire body of state rates has been upheld as to some carriers while being held confiscatory as to another carrier, as in the *Minnesota Rate Cases*, 230 U. S. 352, 469-473. There is usually in a given rate group a weak carrier which operates under such disadvantages and enjoys so little traffic that it cannot earn a fair return on any body of rates practicable in competitive territory. Such a result as was reached in the *Minnesota Rate Cases* in respect of the Minneapolis & St. Louis Railroad Company might be avoided if the charge of confiscation were met by the available showing of the inability of the road to earn a fair return under any reasonable rates. See *Darnell v. Edwards*, 244 U. S. 564, 570, in which it was held that the fact that a road was unwisely built, in a locality where there is not sufficient business to sustain it, might be considered. However, no conclusion properly follows from the result mentioned in the *Minnesota Rate Cases*, except that one carrier had made out a case of inadequate return, and therefore confiscation, while the other carriers had failed to prove their case. We argue at length under the following Point II, sub-point (a), of this brief that the inadequacy of return on the entire property of a carrier resulting from rate regulation is

not the sole ground of complaint against such regulation, that, regardless of the adequacy of the entire return, arbitrary and unreasonable rate regulation is void for want of due process of law, and that an adjustment of rates governed by the amount of net railway operating income of the carriers as the sole and conclusive consideration would be so arbitrary and unreasonable as to be void. That argument and the authorities cited for its support are conclusive of the unsoundness of the legal premise under consideration.

The premise of fact involved in this argument is that it would be *practicable*, through the means of prescribing different rates for different carriers, to effect a limitation of the incomes of carriers to a selected rate of return. It is true that this fact premise is not asserted by the advocates of this law. On the contrary it is universally conceded to be impracticable to apply different rates for different roads on competitive business, for the entire traffic would seek the road charging the lowest rate and the result would be that the strong road would enjoy increased prosperity by reason of the increased volume of business. We submit, however, that the premise of fact stated is necessarily involved in the argument under consideration, and that the admission that the operation of an economic law prevents the making of different rates for different roads destroys the argument. The argument is that the carriers have no ground for complaining of the income-appropriation provisions of this statute because they merely accomplish a result—the limitation of the incomes of

carriers to a selected rate of return—which could be accomplished through the means of different rates for different roads. We say that this argument necessarily means not only that the same result could, as a *matter of law*, be accomplished through the means of different rates, but also that it could, as a *matter of fact*, be accomplished through such means. Now, it is perfectly impracticable to accomplish the same result through the prescribing of different rates, because such difference in rates would immediately cause so radical a change and diversion in the flow of traffic and in the relative volume of traffic carried by the various participating lines that the object sought would be wholly defeated. The prosperous roads would thereby be made more prosperous and the weak roads would be ruined. When this is admitted, the argument is reduced to the proposition that the carriers have no ground for complaining of the income-appropriation provisions because they merely accomplish a result which might *legally* be accomplished by prescribing different rates for different roads, *if it were practicable* to adopt that course, which the advocates of this argument admit that it is not. In other words, we are asked in this argument to assume a purely imaginary result, as a result of the operation of differentiated rates for different roads—to assume that such rates would cause no change in the flow of traffic, and to assume that the carrier limited to the lower rate would neglect all available means of increasing its net income, such as by reduction of operating expenses, or by more intensive solicitation, or by the attraction of improved service.

But if both the premise of law and the premise of fact, above stated, be admitted, the conclusion drawn therefrom is unsound. That conclusion is, that because the limitation of carrier incomes to a selected rate of return could be accomplished through rate regulation, the same object may be accomplished by any other method, without resorting to rate regulation. In other words, the conclusion has for its basis the obviously unsound assumption that whatever result may be brought about, or whatever purpose may be accomplished, as one of the effects, direct or incidental, of the exercise by Congress of a constitutional power, the same may be effected, *without the exercise of the power*, by the short-cut method of direct legislation. The mere statement of this assumption is sufficient to show its unsoundness. If Congress were without power to regulate the issuance by state banks of notes to circulate as money, an act directly prohibiting such issuance of notes could not be sustained by showing that the same result might have been attained through the exercise by Congress of its taxing power. When Congress was without power to restrict or regulate the sale of intoxicating liquors, an act directly restricting or regulating such sale could not have been saved by showing that the same amount of restriction or regulation might have been effected by the exercise of the power of Congress to levy excise taxes. A man may be hanged in this country only according to law. If Congress desires to condemn any carrier to an income not in excess of what Congress deems to be a fair rate of return, it must do so

through the exercise of some one of its constitutional powers. It cannot do so by legislative appropriation and sustain such legislation on the ground that the same result could have been attained by the exercise of its power to regulate interstate commerce or by the exercise of some other power.

The arbitrary character of the income-appropriation provisions appears to be emphasized rather than mitigated by this different-rate theory.

(h) The *New England Divisions* case is plainly distinguishable.

The *New England Divisions* case, 261 U. S. 184, concerned an order of the Commission made under the authority of Section 15 (6) of the Interstate Commerce Act, as amended by the Transportation Act, which order increased the divisions of the New England carriers in joint freight rates participated in by them with the carriers operating west of the Hudson river. It was held that the amendment of the section as to divisions authorized the consideration of the financial needs of particular carriers so as to maintain them in effective operation as a part of an adequate transportation system in the general public interest. In other words, the promotion of the transportation interests of the country as a whole was a purpose of the amendment of the law concerning divisions, just as it was the purpose of the new rate-making provisions of Section 15a. This court said, at page 191: "To accomplish this two 'new devices were adopted: the group system of rate-

"making and the division of joint rates in the public interest." It was contended in that case that if the Act were construed in accordance with the above-stated holding of the Court it was unconstitutional in that the division of a joint rate is essentially a partition of property, that the rate must be divided on the basis of the services rendered by the several carriers and that a division otherwise based was equivalent to the taking from a carrier of a part of the cash in its treasury. This contention was rejected by this Court, holding that the division of a joint rate was not to be determined by mileage alone or cost of service alone. General rate increases for all groups had previously been authorized and the subsequent order as to divisions had the effect of further increasing the revenues of the New England carriers and correspondingly diminishing the increase of revenues which would otherwise have resulted to the other carriers in the eastern group from the previous general increase. This Court said, at page 196: "No part of the revenues needed by the New England lines is paid by the western carriers. All is paid by the community pursuant to the single rate increase ordered in *Ex Parte 74*." It was reasoned that the order as to divisions might properly be deemed a supplement to, or modification of, the order by which the general rate increases had been effected.

The difference between the *New England Divisions* case and the present case is fundamental. The subject-matter dealt with by Congress and by the Commission in the matter of divisions was rates, specifically. The

regulation of divisions affected the revenues of the carriers, but it did so by means legitimate for the government to exercise. The reduction of revenues of certain carriers by modifying the divisions of joint rates affected their revenues in precisely the same way that revenues are affected by reductions of individual rates; both in law and in fact the principle is the same. The operation of the regulation was thus to affect the revenues before they came into being, before the service was rendered and the revenues were earned. Finally, it was the gross revenues which the regulations affected directly, and not the net railway operating income, which can be determined only after the service is rendered and the expenses and losses are charged against the gross revenues. The income-appropriation provisions of Section 15a, quite to the contrary, involve no regulation of rates, either joint or individual, do not make any provision which arrests or prevents the receipt of the revenue, but, after the service has been performed under the lawful rates and under the lawful divisions, and after the revenues have been received and in the processes of accounting have been charged with the expenses and losses of the railroad operations, attempt directly to take from the carriers an amount which can be ascertained only after the operations and accounting mentioned have been completed.

The holding in the *New England Divisions* case that it is within the power to regulate commerce to authorize the Commission to take into consideration, in establishing divisions of joint rates, the financial needs

of particular carriers because of the general public interest in an adequate transportation system, cannot be stretched to the extreme of sanctioning a direct appropriation of income earned by the carriers, on the theory that such action will promote the general public interest through the maintenance of an adequate transportation system. In the first place, the appropriation of such income has no tendency whatever to promote the public interest; the amount paid by the public for its transportation is not reduced and the transportation facilities of the whole country are not increased thereby. In the second place, even if the appropriation of income had some tendency to promote the said public purpose, it would not be within the power of Congress to promote that purpose by a direct appropriation of income (property), as is attempted by this statute, in contradistinction to accomplishing the purpose through an exercise of its power to regulate some part of interstate commerce.

In the *New England Divisions* case, at page 191, the Court, referring to the group system of rate-making, said: "Through the former, weak roads were to be 'helped by recapture from prosperous competitors of 'surplus revenues.'" We think the quoted expression was an inadvertence due to the fact that the provisions of Section 15a were not litigated in that case and so were not the subject of careful analysis. We show under a subsequent heading of this brief that the income appropriated for the purposes of the general railroad contingent fund is not devoted to the assistance of the weak carriers.

POINT II.

The income-appropriation provisions cannot be sustained as a regulation of rates.

The provisions of paragraphs (2), (3) and (4) of Section 15-*a* undoubtedly constitute a regulation of rates in that they direct that rates be made upon a group basis, that they be calculated to produce a certain standard of net railway operating income and that the transportation needs of the whole country be considered. But the present question concerns, not the above cited paragraphs, but paragraphs (5) and (6) *et seq.*—the income-appropriation provisions.

(a) Considering the income-appropriation provisions as attempted rate regulation, on the theory of a seizure of the proceeds of rates impliedly declared to be unreasonable, they are void because of their want of due process of law, in that the amount of net income is arbitrarily made the sole and conclusive measure of the unreasonableness of the rates.

It has been argued by the advocates of these provisions that the *group rates* made by the Commission under the direction of paragraphs (2) to (4) might be considered as merely tentative, as far as each individual carrier is concerned, until the net railway operating income realized by such carrier from said rates is known and that if and when it develops that such income exceeds a 6 per cent. return, the excess may be considered as never having become the absolute property of the carrier but as having been allowed to come

into its possession only conditionally or impressed with a trust, because such excess was the product of rates which were *pro tanto* unreasonable *ab initio*.

There is nothing "tentative" in character about the rates prescribed by the Commission under Section 15a. The attempt to create a tentative status concerns only the net railway operating income.

But it is unnecessary to the theory above stated to characterize the rates as "tentative" or the receipt and possession of the earnings as "conditional" and as "in trust" or their recovery as a "recapture". These terms are used merely to add color to the picture. If rates are unreasonable, the unreasonable portion has always been recoverable from the carrier after its collection of the charges, even at common law. They are, and always have been, unlawful exactions in so far as they exceed what is reasonable. All that it is necessary to read into these paragraphs to carry out the theory invoked for their support, as far as the essential principle of the theory is concerned, is a declaration that, notwithstanding the rates have been prescribed by the Commission as reasonable for the group, they shall be deemed unreasonable as to a particular carrier to the extent that the carrier earns therefrom a return exceeding 6 per cent. That is absolutely all there is to this theory. The fact that Section 15a contains no express declaration to the foregoing effect will be considered under a subsequent subheading hereof. But, assuming that the section is to be construed as embodying by implication a declaration that the group rates shall be deemed un-

reasonable and excessive as to a particular carrier to the extent that the carrier derives therefrom a return in excess of 6 per cent., the question is presented whether such attempted rate regulation is within constitutional limits.

The showing of inadequacy of return on the property used in the public service is not the sole ground of complaint available to the carrier against governmental action, adopted under the guise of rate regulation. The power to regulate rates must not be exercised in an arbitrary and unreasonable manner, and an exercise of alleged rate regulation may be so arbitrary and unreasonable as to transcend the power of Congress, regardless of the fact that from the entire body of rates the carrier derives an adequate return upon its property. The foregoing proposition is established by the following decisions, without attempting to make the citations on this point exhaustive.

The case of *Northern Pacific Railway Co. v. North Dakota*, 236 U. S. 585, concerned a law fixing maximum intrastate rates on coal in carloads. The evidence based on a year's trial of the rates showed that, with proper allocation of expenses to this traffic, the Northern Pacific derived in the year a net profit of only \$847 from this coal traffic out of a total revenue of \$58,953 from such traffic, which this Court considered so small as to be nominal and non-compensatory. The State Court had held it necessary to be shown in order to invalidate this coal rate, that any deficit under the coal rate reduced the net of all intrastate freight earnings

to a point where they were insufficient to afford an adequate return on the property. This Court said at pages 595 and 596: "The fact that the property is devoted to a public use on certain terms does not justify the requirement that it shall be devoted to other public purposes, or to the same use on other terms, or the imposition of restrictions that are not reasonably concerned with the proper conduct of the business according to the undertaking which the carrier has expressly or impliedly assumed. If it held itself out as a carrier of passengers only, it cannot be compelled to carry freight. As a carrier for hire, it cannot be required to carry persons or goods gratuitously. The case would not be altered by the assertion that the public interest demanded such carriage. The public interest cannot be invoked as a justification for demands which pass the limits of reasonable protection and seek to impose upon the carrier and its property burdens that are not incident to its engagement. *In such a case, it would be no answer to say that the carrier obtains from its entire intrastate business a return as to the sufficiency of which in the aggregate it is not entitled to complain.* Thus, in *Lake Shore & Michigan Southern Ry. v. Smith*, 173 U. S. 684, the regulation as to the sale of mileage books was condemned as arbitrary without regard to the total income of the carrier. Similarly, in *Missouri Pacific v. Nebraska*, 217 U. S. 196, it was held that the carrier could not be required to build mere private connections, and the adequacy of the receipts

"from its entire business did not enter into the question.
 "And this was so because the obligation was not involved
 "in the carrier's public duty and the requirement went
 "beyond the reasonable exercise of the State's pro-
 "tective power." And at page 598: "The State insists
 "that the enactment of the statute may be justified as
 "a 'declaration of public policy'. In substance, the argu-
 "ment is that the rate was imposed to aid in the develop-
 "ment of a local industry and thus to confer a benefit
 "upon the people of the State. * * * But, while
 "local interests serve as a motive for enforcing reason-
 "able rates, it would be a very different matter to say
 "that the State may compel the carrier to maintain a
 "rate upon a particular commodity that is less than
 "reasonable, or—as might equally well be asserted—to
 "carry gratuitously, in order to build up a local enter-
 "prise. That would be to go outside the carrier's under-
 "taking, and outside the field of reasonable supervision
 "of the conduct of its business, and would be equivalent
 "to an appropriation of the property to public uses upon
 "terms to which the carrier had in no way agreed. It
 "does not aid the argument to urge that the State may
 "permit the carrier to make good its loss by charges for
 "other transportation. If other rates are exorbitant,
 "they may be reduced. Certainly, it could not be said
 "that the carrier may be required to charge excessive
 "rates to some in order that others might be served at
 "a rate unreasonably low." And at pages 599 and 600:
 "Frequently, attacks upon state rates have raised the
 "question as to the profitableness of the entire intrastate

"business under the State's requirements. *But the decisions in this class of cases* (which we have cited "in the margin) *furnish no ground for saying that the State may set apart a commodity or a special class of traffic and impose upon it any rate it pleases, provided only that the return from the entire intrastate business is adequate.*" And finally at page 601: "It has repeatedly been assumed in the decisions of this court, that the State has *no arbitrary power over the carrier's rates* and may not select a particular commodity or class of traffic for carriage without reasonable reward."

See also: *Lake Shore & Michigan Southern Railway Co. v. Smith*, 173 U. S. 684, the bearing of which on the present point is not affected by its overruling in part by *Pennsylvania R. R. Co. v. Towers*, 245 U. S. 6. *Atlantic Coast Line R. R. Co. v. North Carolina Corporation Commission*, 206 U. S. 1. *Norfolk and Western Railway Co. v. West Virginia*, 236 U. S. 605. *Southern Pacific Company v. Interstate Commerce Commission*, 219 U. S. 433. *Southern Railway Co. v. St. Louis Hay Co.*, 214 U. S. 297. *Chicago, Milwaukee & St. Paul Railroad Company v. Wisconsin*, 238 U. S. 491, which although not strictly a case of rate regulation, was so closely related to such regulation as to be pertinent here. *Interstate Commerce Commission v. Stickney*, 215 U. S. 98, 109.

In some of the cases above cited no discussion occurred of the adequacy of the return of the carrier from its entire business, but in each of them it is clear

that the principle of arbitrary action on which the case was decided would have rendered any showing as to the adequacy of the whole return entirely irrelevant.

The foregoing cases establish that, regardless of the adequacy of the percentage of return upon the whole business, attempted rate regulation will be held void if it is arbitrary and unreasonable. Considering, then, the income-appropriation provisions as implying a declaration that the rates prescribed by the Commission for a group shall conclusively be deemed unreasonable as to a carrier which derives a greater return therefrom than 6 per cent., we submit that such a regulation would be void as lacking due process of law. No action conceivable under the guise of rate regulation could be more unreasonable and arbitrary than a declaration that rates concededly valid and reasonable as to average carrier, in prosperity or earning ability, of a group, and reasonable for the shipper to pay to such average carrier, shall *conclusively* be deemed unreasonable as to a carrier earning a greater return than that fixed as proper for the average carrier, and that the earning of such greater return shall be absolutely the *only evidence* considered, to the exclusion of every consideration and factor which from time immemorial have been judicially held pertinent upon an issue of the reasonableness of rates.

Legislative fiat cannot under our constitutional government accomplish this purpose. The attempt would square only with a system of government subject to no constitutional restraints. The carriers in engaging in

interstate commerce have subjected themselves to the power of Congress to regulate interstate commerce and that power of regulation includes the power to regulate their transportation rates. But the carriers have not subjected themselves to action, under the guise of rate regulation, which either so reduces their compensation as a whole as to amount to confiscation, or is otherwise so arbitrary and unreasonable as to be wanting in due process of law. We assert that a declaration that the amount of the net railway operating income, and that consideration alone, shall be conclusively determinative of the unreasonableness of rates would be so unreasonable and arbitrary on its face as to be void in conflict with the Fifth Amendment, quite independently of any question of confiscation.

Legislative action of this extreme type, in the exercise of the power to regulate commerce, is naturally so nearly unprecedented that few pertinent decisions are available. We think, however, that the following citations fully establish the proposition last above stated.

In *Cotting v. Kansas City Stock Yards Co.*, 183 U. S. 79, there was involved the validity of a statute of Kansas defining public stock yards and regulating the charges thereof. The statute declared that any stock yard having an average daily receipt of a specified number of head of livestock should be deemed a *public* stock yard. The charges by public stock yards were fixed at 15 cents per head for cattle and other specified amounts for calves, hogs and sheep. Mr. Justice Brewer writing the opinion held that the public had acquired an interest

in the stock yards so that the business was subject to governmental regulation within the principle of *Munn v. Illinois*, 94 U. S. 113. The lower court (82 Fed. 850, 856) had found that the net income would be reduced by the state rates about 50% and that the reduced rates would yield a return of 5.3 per cent. on the value of the property, but the lower court was not prepared to hold that the statute was confiscatory and had therefore dismissed the bill. Mr. Justice Brewer suggested various reasons which might justify a distinction between the extent of the regulation applicable in the case of one who has voluntarily undertaken to perform a public service, like a common carrier, and that applicable to one who is not engaged in a public service but has merely devoted his property to a use in which the public has an interest, to which latter class the stock yards belonged. We do not understand, however, that his conclusion in the case was in any way dependent upon this distinction, but rather that he applied to the stock yards there involved what he considered to be the law applicable to those engaged in a distinctly public service. He said at page 95: "Pursuing this thought, we add that "the State's regulation of his charges is not to be measured by the aggregate of his profits, determined by the "volume of business, but by the question whether any "particular charge to an individual dealing with him is, "considering the service rendered, an unreasonable ex- "action. In other words, if he has a thousand transac- "tions a day and his charges in each are but a reason- "able compensation for the benefit received by the party

"dealing with him, such charges do not become unrea-
 "sonable because by reason of the multitude the aggre-
 "gate of his profits is large. The question is not how
 "much he makes out of his volume of business, but
 "whether in each particular transaction the charge is
 "an unreasonable exaction for the services rendered.
 "He has a right to do business. He has a right to
 "charge for each separate service that which is reason-
 "able compensation therefor, and the legislature may
 "not deny him such reasonable compensation, and may
 "not interfere simply because out of the multitude of
 "his transactions the amount of his profits is large. Such
 "was the rule of the common law even in respect to
 "those engaged in a quasi public service independent of
 "legislative action. In any action to recover for an
 "excessive charge, prior to all legislative action, who-
 "ever knew of an inquiry as to the amount of the total
 "profits of the party making the charge? Was not the
 "inquiry always limited to the particular charge, and
 "whether that charge was an unreasonable exaction for
 "the services rendered?" After quoting at length from
 the opinion in *Transportation Company v. Parkersburg*,
 107 U. S. 691, and the opinion of Lord Chancellor Sel-
 borne in *Canada Southern Railway Co. v. International*
Bridge Company, 8 Appeal Cases, 723, his opinion pro-
 ceeded at page 97: "The authority of the legislature to
 "interfere by a regulation of rates is not an authority
 "to destroy the principles of these decisions, but simply
 "to enforce them. Its prescription of rates is *prima*
 "*facie* evidence of their reasonableness. In other words,

"it is a legislative declaration that such charges are
"reasonable compensation for the services rendered, but
"it does not follow therefrom that the legislature has
"power to reduce any reasonable charges because by
"reason of the volume of business done by the party he
"is making more profit than others in the same or other
"business. The question is always not what does he
"make as the aggregate of his profits, but what is the
"value of the services which he renders to the one seek-
"ing and receiving such services. Of course, it may
"sometimes be, as suggested in the opinion of Lord
"Chancellor Selborne, that the amount of the aggregate
"profits may be a factor in considering the question of
"the reasonableness of charges, but it is only one factor,
"and is not that which finally determines the question
"of reasonableness. Now, the controversy in the Cir-
"cuit Court proceeded upon the theory that the aggre-
"gate of profits was the pivotal fact. To that the testi-
"mony was adduced, upon it the findings of the master
"were made, and in recognition of that fact the opinion
"of the court was announced. Obviously, as we think,
"in all this the lines of inquiry were too narrowly pur-
"sued." Mr. Justice Brewer then referred to the find-
ing that the charges made by this stock yard company
were no greater (and in many instances less) than
those of any other stock yard in the country and to the
fact that the charge made by the company per head of
live stock handled was so small as to suggest no extor-
tion. While concluding, therefore, that the lower court
had proceeded upon too narrow lines, as indicated in

the above quotations, the decision was rested upon another ground. It appeared that the Kansas City Stock Yards Co., party to this suit, was the only stock yard company to which the statute applied in view of its declaration that only those stock yards having an average daily receipt of a specified number of head of live stock should be deemed *public* stock yards. The statute was therefore characterized, page 103, as attempting a classification "between stock yards doing a large and those "doing a small business". And on this subject it was said, page 104: "Clearly the classification is based solely "on the amount of business done and without any reference to the character or value of the services rendered. "Kindred legislation would be found in a statute like "this: requiring a railroad company hauling ten tons or "over of freight a day to charge only a certain sum "per ton, leaving to other railroad companies hauling "a less amount of freight the right to make any reasonable charge; or, one requiring a railroad company "hauling a hundred or more passengers a day to charge "only a specified amount per mile for each, leaving "those hauling ninety-nine or less to make any charge "which would be reasonable for the service; or (if we "may indulge in the supposition that the legislature has "the right to interfere with the freedom of private contracts), one which would forbid a dealer in shoes and "selling more than ten pairs a day from charging more "than a certain price per pair, leaving the others selling "a less number to charge that which they deemed reasonable; or forbidding farmers selling more than ten

"bushels of wheat to charge above a specified sum per bushel, leaving to those selling a less amount the privilege of charging and collecting whatever they and the buyers may see fit to agree upon. In short, we come back to the thought that the classification is one not based upon the character or value of the services rendered but simply on the amount of the business which the party does, and upon the theory that although he makes a charge which everybody else in the same business makes, and which is perfectly reasonable so far as the value of the services rendered to the individuals seeking them is concerned, yet if by the aggregation of business he is enabled to make large profits his charges may be cut down. The question thus presented is of profoundest significance. Is it true in this country that one who by his attention to business, by his efforts to satisfy customers, by his sagacity in discerning probable courses of trade, and by contributing of his means to bring trade into those lines, succeeds in building up a large and profitable business, becomes thereby a legitimate object of the legislative scalping knife?" And it was held that this statute did not embody a classification based upon inherent differences in the character of the business but was discrimination between persons engaging in the same class of business and based simply upon the quantity of business which each did and that therefore it was void as a violation of the equal protection clause of the Fourteenth Amendment.

The court was unanimous in its judgment. Mr. Chief Justice Fuller and Mr. Justice Peckham concurred in the opinion of Mr. Justice Brewer. The six remaining Justices, it is true, concurred only upon the ground that the statute was a violation of the equal protection clause and deemed it unnecessary to express an opinion whether the statute was unconstitutional upon the further ground that by its necessary operation it would deprive the stock yards company of its property without due process of law. It does not appear to us that this fact detracts from the weight of the decision as an authority bearing on the present question. The effect of paragraphs (5) and (6) of Section 15a, now under consideration, viewed as a rate regulation, is to attempt a classification for rate regulation of the same character as that condemned in the *Cotting* case. After prescribing for the Commission a rule of rate making on the group basis, the effect of this statute, as it is contended by its supporters, is to make the rates so prescribed unreasonable and unlawful as to those carriers which earn therefrom a return in excess of 6 per cent., while leaving the same rates reasonable and lawful for all other carriers, even as applied to the same traffic between the same points of origin and destination. The earning of a return in excess of 6 per cent. will depend largely upon the greater volume of business carried and so will be on all fours with the classification condemned in the *Cotting* case. To some extent the earning of such excess will be the result of other factors, such as more economical and efficient operation, and it

cannot be doubted that a classification based upon such factors and penalizing such greater economy and efficiency is more vicious than a classification based simply upon volume of business. The arbitrariness of such classification is emphasized when, as here, the classification is not for the purpose of determining rates for the future but is for the purpose of regulating for a past period the rates under which the carriers have conducted their business. It is true that, strictly analyzed, the decision in the *Cotting* case was based upon the violation of the equal protection clause of the Fourteenth Amendment. But the distinction between a denial of equal protection and a denial of due process is a shadowy one. While the spheres of protection afforded by the equal protection and due process clauses are not co-terminous, "the violation of one may involve at times the violation of the other". *Truax v. Corrigan*, 257 U. S. 312, 322. Considering that it is well established law that, in the exercise of its power to regulate rates, Congress may not act unreasonably and arbitrarily, we submit that the arbitrary classification here presented, for rate-regulation purposes, if this be deemed rate-regulation, amounts to a deprivation of property without due process of law. And, aside from the ground on which the decision in the *Cotting* case was definitely based, the reasoning of Mr. Justice Brewer, concurred in by the Chief Justice and Mr. Justice Peckham, upon the broader ground so commends itself by its logic and forcefulness as to be entitled to the weight of an actual decision of the Court.

In *Canada Southern Railway Co. v. International Bridge Co.*, English Law Reports, 8 Appeal Cases 723, the Judicial Committee of the Privy Council affirmed an appeal from the Court of Appeal of the Province of Ontario, Dominion of Canada. One question involved was the reasonableness of the charges imposed by the bridge company for the use of the bridge by railroad trains. It was considered that the statute governing the bridge left such charges to be fixed by the bridge company with no other limitation than that implied by law that the charges should not be unreasonable. Lord Chancellor Selborne said, page 731: "It certainly appears to their Lordships that the principle must be, when reasonableness comes in question, not what profit it may be reasonable for a company to make, but what it is reasonable to charge to the person who is charged. That is the only thing he is concerned with. They do not say that the case may not be imagined of the results to a company being so enormously disproportionate to the money laid out upon the undertaking as to make that of itself possibly some evidence that the charge is unreasonable, with reference to the person against whom it is charged. But that is merely imaginary. Here we have got a perfectly reasonable scale of charges in everything which is to be regarded as material to the person against whom the charge is made. * * * That being so, it seems to their Lordships that it would be a very extraordinary thing indeed, unless the legislature had expressly said so, to hold that the persons using the bridge could claim a

"right to take the whole accounts of the company * * *
 "to ask a Court to say that the persons who have pro-
 "jected such an undertaking as this * * * are to
 "be regarded as making unreasonable charges, not be-
 "cause it is otherwise than fair for the railway company
 "using the bridge to pay those charges, but because the
 "bridge company gets a dividend which is alleged to
 "amount, at the utmost, to 15 per cent. Their Lord-
 "ships can hardly characterize that argument as any-
 "thing less than preposterous." It is pertinent to com-
 ment that the references in the above quotation to the
 possibilities of the legislature expressly so directing, of
 course contemplated a legislature not subject to the
 constitutional limitations which restrict the action of
 the Congress of the United States.

The complementary proposition that the inability of
 the carrier to make a profit from reasonable rates does
 not justify it in charging unreasonable rates is fully
 recognized and established. The two propositions stand
 together. If the rates are reasonable from the stand-
 point of the value of the service, they cannot be reduced
 simply because the carrier realizes a large profit there-
 from and they cannot be increased simply because the
 carrier is unable to realize a profit therefrom.

In *Covington Turnpike Co. v. Sandford*, 164 U. S.
 578, the Turnpike Company resisted tolls prescribed by
 the State legislature as unreasonable and unjust to the
 company and its stockholders in that the resulting reve-
 nue was insufficient for the upkeep of the roads and
 for dividends. This court said, at page 596: "But

"that involves an inquiry as to what is reasonable and
 "just for the public. If the establishing of new lines
 "of transportation should cause a diminution in the
 "number of those who need to use a turnpike road, and,
 "consequently, a diminution in the tolls collected, that
 "is not, in itself, a sufficient reason why the corporation
 "operating the road should be allowed to maintain rates
 "that would be unjust to those who must or do use its
 "property. The public cannot properly be subjected to
 "unreasonable rates in order simply that stockholders
 "may earn dividends. * * * If a corporation cannot
 "maintain such a highway and earn dividends for stock-
 "holders, it is a misfortune for it and them which the
 "Constitution does not require to be remedied by im-
 "posing unjust burdens upon the public."

In *Reagan v. Farmers Loan & Trust Co.*, 154 U. S. 362, this Court said, at page 409: "They who invest
 "their money in railroads take the same chances that
 "men engaged in other business do of making profit
 "from the carrying on of their business; and, as ap-
 "pears from other cases submitted to us with this, some
 "of the railroads in the State of Texas have been
 "operated at a constant loss. But such possibilities of
 "loss are simply the natural results of all business freely
 "carried on, against which the law is powerless to afford
 "protection."

Interstate Commerce Commission v. Union Pacific R. R. Co., 222 U. S. 541, at page 549, the Court said:
 "But whether the carrier earned dividends or not sheds
 "little light on the question as to whether the rate on a

"particular article is reasonable. For, if the carrier's "total income enables it to declare a dividend, that "would not justify an order requiring it to haul one "class of goods for nothing, or for less than a reason- "able rate. On the other hand, if the carrier earned no "dividend, it would not have warranted an order fixing "an unreasonably high rate on such article."

In *Hooker v. Interstate Commerce Commission*, 188 Fed. 242, the Commerce Court reviewed an order of the Commission fixing certain rates, the petitioners in the suit being shippers who complained that the rates were extortionate. One of the carriers participating in the traffic was the Cincinnati, New Orleans and Texas Pacific Railway Co. The case against the rates was almost entirely based upon the large earnings of that road. It was alleged that if the rates fixed by the Commission had been applied during the preceding five-year period the average net earnings of that road on its capital stock would have been over 40 per cent. The Commission, however, had held that it was not at liberty to fix rates solely with reference to the C. N. O. & T. P., but must fix them with reference also to other companies which would necessarily be affected, that it should establish rates which were just and reasonable for the *section* in which they prevail. The Commerce Court said at page 251: "It appears from the findings of the "Commission that it has always refused in the consid- "eration of the reasonableness of a rate or rates to con- "sider only the particular carrier making the same by "itself, but on the contrary has always considered the

"rates in a particular territory or the rates of other
"carriers to be affected by the change of the particular
"rate or rates in question; and we think it fair to say
"that, so far as the Commission is concerned, there has
"been a uniform policy, public policy if you please, be-
"cause the Commission represents the United States in
"so far as it acts within the scope of its delegated au-
"thority in the establishment of reasonable and just
"rates, to the effect that it will not fix rates or determine
"their reasonableness solely upon a consideration of the
"particular carrier whose rates are directly involved.
"We think this court may take judicial knowledge of
"the fact that the interstate rates prescribed for the
"transportation of freight by common carrier must nec-
"essarily be more or less interdependent, or at least be
"so related to each other that the rate-making power
"will not, simply because it has the power, fix a rate
"upon a single line of railroads which will necessarily
"disorganize established and reasonable rates on other
"railroads in the same territory." And it was further
said, page 253: "The Commission found that the rates
"complained of were not clearly excessive. Much less
"are we able to find that the rates authorized by the
"Commission in the order complained of and which
"were a reduction of the former rates are clearly ex-
"cessive. In making this statement we are fully aware
"of the allegation of the bill as to the net earnings of
"the C. N. O. & T. P., and the whole case as to the ex-
"cessive feature of the rates fixed by the Commission
"is almost entirely based upon the earnings of the C.,

"N. O. & T. P. While earnings may be considered in
 "the fixing of a reasonable rate to be charged by a car-
 "rier for the transportation of freight, rates necessarily
 "cannot be based upon earnings alone. This is made
 "clearly to appear when we consider that a just and rea-
 "sonable rate is one which is just to the carrier and to
 "the shipper. It is a rate which yields to the carrier a
 "fair return upon the value of the property employed in
 "the public service, and it is a rate which is fair to the
 "shipper for the service rendered; and when this rate is
 "established, if it results in large profits to the carrier,
 "the carrier is fortunate in its business, and if it results
 "in a loss of earning power so that the business of the
 "carrier is unprofitable the carrier is unfortunate. But
 "the rate may not be lowered or raised merely upon the
 "ground that the carrier is either making or losing
 "money, providing always the rate is a reasonable and
 "just rate. Indeed, it has been held that the earning
 "power of the rate is one of the least considerations in
 "fixing a just and reasonable rate."

Receivers and Shippers Association v. Cincinnati, New Orleans and Texas Pacific Railway Company, 18 I. C. C. 440, was the decision of the Commission reviewed by the Commerce Court in the *Hooker* case above cited. The Commission's report states that since 1899 the C., N. O. & T. P. had paid the stipulated rental for a line leased by it and had shown very handsome returns from operation as well, that the property was unique among railroads in the south, that its gross earnings per mile for the year 1907 were over \$26,000, being

more than the average gross of the railroads in any group in the United States, that its grades were heavy and cost of operation and maintenance high but that nevertheless its net earnings had for several years reached \$7,000 per mile. The Commission said, page 461: "If it is our duty to take this railroad by itself and "to determine the reasonableness of these rates by a "reference to cost of construction, cost of maintenance, "and profit upon the investment, we think the com- "plainants have established their case and that these "rates ought fairly to be reduced * * *." And further at page 462: "The defendants also contend that "these rates should be fixed not only with reference to "the financial results and the financial necessities of the "Cincinnati, New Orleans & Texas Pacific Company, "but also with reference to other companies whose rates "are necessarily affected by these; otherwise stated the "Commission should establish rates which are just and "reasonable for the section in which they prevail; if a "particular company is so situated that it can make a "handsome profit under such rates, that is the good fortune of that company just as it would be the misfortune of some other company if it could not show as "favorable earnings." And the Commission held that considering the interests of the whole territory there was no occasion for a wide-spread reduction in rates and that the rates themselves were not clearly excessive. A slight reduction was made, but substantially the relief sought by the complainant was denied.

In *Railroad Commissioners of Iowa v. Illinois Central Railroad Company*, 20 I. C. C. 181, the State Board of Railroad Commissioners complained of the charges made for the carriage of passengers over the Dubuque-East Dubuque Bridge by the Illinois Central controlling the bridge. It appeared that the net earnings of the bridge were about 20 per cent. on its original cost, although the Commission considered that a part of this profit was merely bookkeeping. The Commission said, page 186: "But the fact that the net revenues of the Illinois Central from its ownership of the bridge, when so estimated, may be greater than the returns on ordinary business enterprises is not sufficient in itself to justify a holding that the bridge tolls are excessive. * * * The net revenues have an undoubted and often an important bearing upon the question of the reasonableness of rates, but the value of the service to the shipper and the other elements so often referred to as entering into the reasonableness of rates must also be taken into consideration. In this connection *Canada Southern Railway Co. v. International Bridge Co.*, 8 App. Cas. 731, is not without interest. A railroad company may be operated with a less return than it ought to enjoy or even at a loss, but neither condition of affairs would justify the exaction by it of rates that are higher than they reasonably should be for services performed, all things being considered. So also the fact that the net earnings of a carrier may be large does not of itself justify us in fixing a rate at less

"than is reasonable for the service, all other things being considered."

It has been recognized by the courts and the Interstate Commerce Commission that a rate may not be confiscatory, that is, so low as to amount to a taking of the carrier's property without just compensation, and yet not constitute a reasonable rate in the sense of yielding an adequate compensation; in other words, that the terms "just and reasonable" are not synonymous with "non-confiscatory". *Union Pacific Railroad Co. v. Kansas Public Utilities Commission*, 95 Kas. 604; *Railroad Commission of Texas v. Houston Texas Central Railroad Co.*, 90 Texas, 340; *Detroit and Mackinac Railway Co. v. Michigan Railroad Commission*, 171 Mich. 335; *Louisiana Railway & Navigation Co. v. Railroad Commission*, 131 La. 387; *Minneapolis, St. Paul & S. Ste M. Ry. Co. v. Wisconsin Railroad Commission*, 136 Wisconsin, 146; *Trier v. Chicago, St. Paul M. & O. Ry. Co.*, 30 I. C. C. 352, 355; *Holmes & Hallozwell Co. v. Great Northern Railway Co.*, 37 I. C. C. 627, 635.

In *Investigation and Suspension Docket No. 26*, 22 I. C. C. 604, the Commission said at page 624:

"We may not say that a rate shall be fixed so as
 "to meet the requirement or needs of any body of
 "shippers in their efforts to reach a given market, nor
 "may we establish rates upon any articles so low that
 "they will not return out of pocket cost. Neither could
 "we fix an entire schedule of rates which would yield
 "an inadequate return upon the fair value of the prop-

"erty used in the service given. There is, however, a
 "zone within which we may properly exercise 'the flex-
 "ible limit of judgment which belongs to the power to
 "fix rates.' These are the words of the Chief Justice of
 "the Supreme Court, 206 U. S. 26. There is no flexible
 "limit of judgment if all rates must be upon a level of
 "cost, and out of every dollar paid to the carrier must
 "come a fixed amount of return for capital invested.
 "The recognition of such a doctrine has never been sug-
 "gested either by Congress or the Supreme Court. A
 "just and reasonable rate must be one which respects
 "alike the carriers' deserts and the character of the
 "traffic. * * * The words 'just and reasonable' imply the
 "application of good judgment and fairness, of common
 "sense and a sense of justice to a given condition of
 "facts. They are not fixed, unalterable, mathematical
 "terms. Their meaning implies the exercise of judg-
 "ment and against the improper exercise of that
 "judgment the Constitution gives protection, at least as
 "far as the carriers are concerned."

(b) But the income-appropriation provisions do not pur-
 port to be and are not a regulation of rates.

The whole argument under sub-heading (a), above,
 is upon the assumption, indulged for the purpose of
 argument, that the provisions for the disposition of the
 net railway operating income in excess of six per cent.
 on the property value can be construed as a regulation
 of rates by reading into, or implying from, those pro-
 visions a declaration that the rates made by the Com-

mission for a group are unreasonable as to any carrier earning therefrom a net railway operating income over 6 per cent. But the provisions in question do not purport to be a regulation of rates and cannot reasonably be construed as such.

The rate regulation is confined to paragraphs (2) to (4) of Section 15a, wherein the rule of rate-making on the group basis is prescribed and the mandate given the Commission to take into consideration the transportation needs of the whole country in fixing the rate of fair return for the groups, etc. Paragraph (5) then, by way of recital, states the opinion that under any rates sufficient to sustain the carriers as a whole some carriers will realize a return "substantially and unreasonably in excess of a fair return", and follows such recital with a provision that the "part of such excess, as hereinafter prescribed," shall be held in trust for and paid over to the United States. This paragraph does not contribute any support to the theory of rate regulation. Its conclusion, or substantive provision, is at most an assertion of a claim in favor of the Government to any excess railway income over a "fair return". Its recital merely explains why the claim is asserted and attempts to justify the claim. The whole paragraph is nothing more than an introduction for paragraph (6). Paragraph (6) provides in brief that any carrier realizing a net railway operating income in excess of 6 per cent. upon its property value shall hold one-half of the excess as a reserve fund for purposes specified in subsequent paragraphs and pay over to the Commission the remain-

ing half of the excess. It is clear that the provision as to income in excess of 6 per cent. is not inferentially a declaration that 6 per cent. on property value is the measure of a "fair return". The percentage of property value constituting a "fair return" is by paragraph (3) definitely prescribed by Congress itself as $5\frac{1}{2}$ per cent. for the first two years, with discretion to the Commission to increase it to 6 per cent. to provide for improvements chargeable to capital account. By the same section the percentage constituting a "fair return" after the expiration of the first two years is to be determined by the Commission. The 6 per cent, adopted for the purpose of paragraph (6) is therefore a fixed basis, arbitrarily selected as a matter of convenience, which may or may not correspond to the "fair return" ascertained as provided in paragraph (3). Congress, while itself prescribing the "fair return" for the first two years and directing the Commission to determine it thereafter, has not undertaken to dispose of *all* net railway operating income in excess of such fair return, but only, in the language of paragraph (5), "such part of the excess, as hereinafter prescribed." The section contains no express declaration that the rates prescribed for a group shall be deemed unreasonable to the extent that they have produced net railway operating income in excess of the $5\frac{1}{2}$ per cent. prescribed as a "fair return" for the first two years, or in excess of such rate as the Commission shall allow as a "fair return" thereafter. It contains no express declaration that the group rates shall be deemed unreasonable to the extent that

they produce a net railway operating income in excess of the 6 per cent. rate used for the purposes of paragraph (6). There is no justification for implying any such declaration. It would be clearly unjustifiable to imply a declaration that the rates were unreasonable to the extent that they produce an income in excess of the "fair return" fixed under paragraph (3), for the omission of Congress to attempt to appropriate or dispose of the whole of that excess is evidently a concession by Congress of the propriety of a carrier retaining *some* net earnings in excess of what is determined to be in the strict sense a "fair return". There remains, as an argument that the income-appropriation provisions constitute rate regulation, only that, since Congress has undertaken to appropriate or control the disposition of the railway income in excess of 6 per cent., it must be inferred that this portion of the railway income in excess of a "fair return" was considered by Congress as "substantially and unreasonably in excess of a fair return", in the language of the recital in paragraph (5), and that therefore there should be implied a declaration that the rates prescribed for the group to the extent that they produce a return in excess of 6 per cent. are unreasonable. But such argument cannot prevail for the reasons and considerations hereinafter stated.

The body of rates for the group which the Commission is directed by paragraph (2) to prescribe is expressly recognized as made or to be made "in the exercise of its power to prescribe just and reasonable rates." The body of rates so prescribed will constitute

the lawful rates and the only lawful rates for the use of every carrier of the group. There will attach to them as complete and conclusive sanction as to reasonableness as if they had been specifically named in an Act of Congress.

The body of rates so prescribed under paragraph 2 must necessarily be reasonable, judged as a whole, for the average carrier of the group—average as to earning capacity, operating cost and property value—for this is in effect the premise of the rate structure of the group. If the rates are reasonable for the average carrier of the group, it is an irresistible conclusion that they are reasonable for all carriers in the same group, including any carrier which is able to realize a net railway operating income constituting a greater percentage, than the average, of its property value.

In *Proposed Advances in Freight Rates* (1903), 9 I. C. C. 382, the Commission said at page 425: "The transportation charge must be the same by all routes. "Whatever rate is made on grain from Chicago to New York by the Vanderbilt System must determine the rate between that point and the Atlantic Seaboard by all routes. Since the fixing of a rate upon that system indirectly determines what that charge shall be upon all other roads, should we, by reason of this indirect effect, consider the condition of those roads? It might be manifestly unfair to select a single advantageous line and make that the standard. We have seen that grain can be transported under actual conditions by the Lake Shore and the New York Central Railroads from

"Chicago to New York at a cost less than that by most other routes. It would be hardly just to these other routes to compel the putting in of a rate upon that line which was reasonable with respect to it alone and which had no reference to its competitors. Upon the other hand, it would be equally unfair to the public if the most expensive line were made the standard."

In *City of Spokane v. Northern Pacific Railway Co.*, 15 I. C. C. 376, the Commission held that the reasonableness of a rate between two points served by two or more carriers could not be determined by consideration alone of that line which is shortest and most favorably situated as to operations, earnings, etc., but that the entire situation must be considered (see particularly pp. 392 to 394).

This principle was reaffirmed in *Kindel v. New York, New Haven & Hartford Railroad Co.*, 15 I. C. C. 555, 561, 563. Referring to the three cases above cited in *Receivers and Shippers Association v. Cincinnati, New Orleans & Texas Pacific Ry. Co.*, 18 I. C. C. 440, the Commission said at page 464: "We have no doubt as to the correctness of this principle and believe it must be applied here within proper limits."

In *Advances in Rates* (1911), 20 I. C. C. 243, considering what roads should be taken as the standard in the determination of rates in official classification territory, the Commission concluded that the Pennsylvania, New York Central and Baltimore & Ohio systems should all be used and said (p. 274): "In 9 I. C. C. Rep. 382,

"this Commission considered the justice of certain advances in grain rates between Chicago and the Atlantic seaboard and it there held that whatever rate might reasonably be imposed upon these three systems must be held to be a reasonable charge for that service by all lines. We hold to the same view in this investigation. We do not mean that other lines should not be considered, but that these systems may be taken as typical. Under rates reasonable for these three systems there may be lines whose earnings will be extravagant, but that is their good fortune. There may be lines which cannot make sufficient earnings, but that is their misfortune. We ought not to impose upon this territory, for the purpose of allowing these defendants additional revenues, higher rates than are adequate to these three systems considered as a whole."

Section 15a contains nothing from which it is justifiable to infer that Congress deemed that the rates fixed with particular reference to the average or typical carrier of the group become unreasonable in the case of a carrier able to realize more than a "fair return" or more than a 6 per cent. return. The appropriation of a part of the excess over a 6 per cent. return and the assumption of control over the balance of that excess does not justify an inference that Congress deemed the rates producing that part of the net railway operating income unreasonable but is absolutely consistent with an entire concurrence by Congress in the view of the Commission, shown in the cases above cited, that the rates fixed with reference to the average or typical carrier are just and

reasonable for all carriers in the territory. All that the provision for appropriating and controlling the disposition of a part of the railway income necessarily indicates is that Congress deemed such income excessive, or as greater than it was willing to allow the carrier to retain, however just and reasonable might be the rates under which it was earned.

There is no provision for a determination by the Commission that the body of rates prescribed for the group is unreasonable as to the carrier realizing an excess over 6 per cent. It would seem that if the intention had been to adopt these provisions as *rate regulation* there would have been inserted a provision for such determination by the Commission as a condition precedent to the recovery by the Government of the excess resulting from rates believed to be unreasonable. Due regard for constitutional procedure would seem to have dictated such a provision. Section 15a is interjected into the Interstate Commerce law as a component part of that law. The provisions of that law (Sec. 15) for the investigation of rates and the adjudication by the Commission of their unreasonableness still stand. The right of the shipper to complain of unreasonable rates and recover reparation has not been taken away, although it may be reduced or limited to the extent that rates in the future are prescribed by the Commission, rather than initiated by the carrier. It is provided in paragraph (17) of Section 15a that the provisions of this section shall not be construed as depriving shippers of their right to reparation but that they shall not be

entitled to reparation on the ground that any particular rate reflects an excess over 6 per cent. recovered by the Government. This expressly saves the former reparation right and merely denies it any enlargement by reason of paragraphs (5) and (6) of Section 15a. This denial to the shippers of a right to assert that rates are unreasonable because they produce a return in excess of 6 per cent. stands in direct opposition to any inference that Congress intended to declare the rates unreasonable to the extent that they produce an income in excess of 6 per cent.

It might occur, in the case of any body of rates prescribed by the Commission for a group that every rate composing that body of rates had been passed upon by the Commission, at the instance of complaints by shippers, and held to be just and reasonable. There is certainly nothing in the law to prevent complaints by shippers as to each and every rate composing the body of rates prescribed for a group and it might well be that over a period of years substantially all of such rates would be separately passed upon by the Commission and adjudged to be just and reasonable. Paragraph (2) expressly reserves to the Commission the power to consider the justness and reasonableness of particular rates prescribed as a part of the body of rates for a group. Nevertheless this law purports to operate as fully in such a case as in any other cases and to take for public purposes the excess earned by the carrier over 6 per cent. This consideration is conclusive against any inference of a declaration by Congress that the rates

producing an income in excess of 6 per cent. are *pro tanto* unreasonable.

In these provisions no distinction has been made between earnings from interstate and earnings from intrastate business. Congress has assumed to appropriate and control the disposition of net railway operating income in excess of a 6 per cent. return realized from the entire business of the carriers. Suppose that a carrier earns from its interstate business, exclusively, a net railway operating income of 5 per cent. If its net railway operating income derived from its intrastate business does not exceed one per cent., its entire income is not affected by these provisions of the statute. But, if from its intrastate business it realizes more than one per cent. of net railway operating income, there will be an excess subject to appropriation and control under the provisions of this law. This consideration presents an additional and very serious obstacle to any theory that these provisions of the law should be construed as a declaration that the rates producing the statutory excess of railway income are *pro tanto* unreasonable, for the rates producing such income are in part intrastate rates, over which Congress has control only to a limited extent and under special conditions. It is well settled that the earnings under interstate rates may not be used in determining the adequacy of the return from intrastate business. *Smyth v. Ames*, 169 U. S. 466, 541.

It seems clear, therefore, beyond the possibility of a doubt, that Congress by these provisions had no intention of condemning as unreasonable the rates producing

a so-called excess income, but that, having required the making by the Commission of rates on a specified basis, it regarded the rates, when so fixed, as reasonable for shippers to pay to all carriers of the group and as reasonable *per se* for all the carriers to apply, and simply sought to prevent the enjoyment of railway incomes which it regarded as excessive by the direct and straightforward method of declaring that the excess belonged to the Government and requiring it to be paid to the Government. In so doing Congress undoubtedly proceeded in the hope that it would be held to be acting within its power to *regulate commerce*, on the theory that the regulation of the incomes of interstate carriers was within that power. The Committee reports show that question had been seriously raised as to the constitutionality of such action. But that Congress believed that it was, by these provisions for the disposition of railway operating income, exercising the power of regulating rates, or intended to invoke this power to sustain its action, there is not the slightest evidence or indication to be discovered in the Act.

(c) To construe the income-appropriation provisions as a regulation of rates would do violence to the whole theory upon which rate regulation rests.

The right of government to regulate the charges for the use of properties impressed with a public trust *rests upon the theory that without such regulation the owner may exact from the individual patrons unreasonably high rates*. In *Lake Shore & Michigan Southern Ry.*

Co. v. Smith, 173 U. S. 684, at page 698, this Court said: "The authority to legislate in regard to rates comes from the power to prevent extortion or unreasonable charges or exactions by common carriers or others exercising a calling and using their property in a manner in which the public have an interest". See also the exhaustive discussion of the origin of this power in *Munn v. Illinois*, 94 U. S. 113, 125-130, 133-4. *The power to regulate rates, therefore, does not rest upon the theory that without such regulation the owner may enjoy an unreasonably large net income.* The origin and purpose of the regulation was the protection of the individual users and not the regulation of the net income of the owner.

Future charges to be paid by individual patrons of a railroad are in no wise affected by the income-appropriation provisions. Under the rates prescribed or approved by the Commission for a rate-making group, the patrons of the road or roads in that group whose income is sufficient to become subject to appropriation under this statute, as well as the patrons of those roads in the group whose income is not subject to appropriation, pay the same rates.

Neither are the charges paid by shippers for past transportation service affected by the income-appropriation provisions. These provisions are not a device by which the patrons of prosperous roads recoup charges paid by them, upon the theory that, as to the services performed by such roads, such charges were unreason-

able. By paragraph (17) of Section 15a it is provided that no shipper shall be entitled to recover reparation upon the sole ground that any particular rate may reflect a proportion of "excess income" payable by the carrier to the Commission. The necessity for this restriction is obvious, for manifestly any attempt to distribute amounts of income appropriated among the shippers who had contributed to that income not only would have been unworkable, but would have defeated the express intent of the Act to maintain uniform rates upon competitive traffic.

The income-appropriation provisions therefore are not a regulation of rates for the future, for the rates to be charged in the future are not affected by these provisions. They are not a regulation of rates charged in the past, through providing a means of making reparation to shippers for rates, assumed to have been excessive, collected from them in the past, for reparation based upon these provisions is expressly denied. They are not within the scope of the historical origin and purpose of rate regulation, or within the limits of rate regulatory powers as understood from the earliest days of common law to the present time, for they do not affect the rates paid by the public, for the future or in the past. It follows necessarily that to construe these provisions as a regulation of rates would do violence to the whole theory upon which rate regulation rests.

(d) The income-appropriation provisions do not acquire the character of a regulation of rates by reason of any interdependence between them and those provisions of the same section which are concededly a regulation of rates.

There is no essential connection, and no necessary interdependence, between the income-appropriation provisions and the rate regulating provisions of Section 15a. We have hereinbefore conceded that the provisions of paragraph (2), (3) and (4) of Section 15a constitute rate regulation. In enacting these rate regulation provisions, Congress had certain objects, namely: (1) to determine the rates to be paid by the public, having in view the transportation needs of the whole country and the necessity of enlarging transportation facilities; (2) to prescribe a method for fixing such rates, the group basis, which would produce revenue adequate to sustain the average roads and probably better the former condition of the weak roads of the group. Paragraphs (5) and (6) *et seq.* had as their object a third and entirely distinct object, namely, to prevent the better-than-average carrier of a group from retaining net income realized from the rates prescribed under the new rule of rate-making in excess of a rate of return fixed by the Act. The first two objects were effected by provisions which concededly have the character of a regulation of commerce. But this cannot be said of the legislation designed to accomplish the third object. Net income of a carrier, although due in part to interstate commerce business, arises after the act of interstate

commerce has been completed. The power to regulate interstate commerce does not persist after such commerce has become a *fait accompli*, and extend to the regulation of the net income derived in part from such commerce. Apprehending an argument of the character just indicated against the power of Congress to accomplish the third object, an effort was made, apparent on the face of the Act, to indicate that the seizure of incomes of carriers in excess of the standard defined is an essential part of an interdependent scheme of rate making. But the effort to establish an essential connection or necessary interdependence between the parts of this section which constitute a regulation of interstate commerce and the part which is not a regulation of such commerce cannot succeed. The regulation of the income of certain carriers by the appropriation of a part of their income will not affect the rates to be paid by the public. The operation of the group plan of rate making, as a means of sustaining the average carriers and bettering the condition of the weak roads, is likewise not affected by the existence or operation of the plan to appropriate a part of the income of the stronger carriers. All that part of Section 15a which is concerned with the rates to be paid by the public and with the adequacy of revenues to sustain the carriers, becomes effective and fulfills its designed purposes before and independently of the operation of the income-appropriation provisions. The omission of the income-appropriation provisions would not have changed the rates to be paid by the public or lessened or altered the designed

benefits to the average and the weak carriers from the group plan of rate making.

It is argued that a scheme of rate making, such as Congress sanctioned in this statute, which provides a living income for the average carrier in a group, will unavoidably afford the strong carriers a more than living income; that the people of this country might not be willing to acquiesce in such a method of making rates unless it were accompanied by an appropriation of the earnings of any carriers in excess of a living income; that the public which pays the rates of the strong carriers demands that such excessive earnings be appropriated by the general Government rather than left to be expended by the carriers, which serve the public, in the improvement of their service and enlargement of their facilities. The foregoing argument states the only conceivable theory of interdependence between the income-appropriation provisions and the rate-making provisions. The supposed attitude of the public may or may not have been correctly forecast. Even if the forecast were correct, there results no interdependence of these provisions which the law can recognize. The desirability of curtailing or controlling or directing the effect of the exercise by Congress of an express power is not sufficient to enlarge the powers of Congress. For example, if Congress should prohibit national banks from establishing branches, the fact that Congress or the public may deem it desirable that national banks should not in this respect be at a disadvantage in their

competition with state banks would not give Congress power to prohibit state banks from having branches.

The income-appropriation provisions are merely a recognition of the following fundamental economic facts: (1) that rates on competitive traffic must be the same for all roads participating; (2) that with the same level of rates competing lines will show varying rates of return upon their property values; and (3) that a level of rates necessary to maintain an efficient transportation service for all of such competitors combined may and probably will result in a rate of return for some carriers in excess of that which might be fixed for them alone as a reasonable rate of return. In undertaking to deal with such assumed excess, Congress was not engaging in rate regulation but simply in an effort to control the product of that regulation. The economic facts upon which the income-appropriation provisions rest existed long before this enactment, and, as evidenced by numerous decisions, cited above, have always been recognized by the Commission in the establishment of rates for competitive traffic under the general requirement of the law that the rates fixed shall be just and reasonable. Under rates thus fixed by the Commission the rate of return of certain carriers in the pre-war period exceeded 6 per cent., as shown by Senate Committee report to which reference has already been made. *If the appropriation of so-called excess income under the provisions of the present statute may be sustained as a regulation of rates or a regulation of*

commerce, then it is clear that it would have been competent for Congress, without providing the rule of rate-making enacted in Section 15(a), to have merely reaffirmed the requirement that all rates should be just and reasonable, left their determination to the Commission, and then provided that any carrier receiving in any year a net income in excess of 6 per cent. on the value of its property should divide such excess with the Government. Such an enactment would have been as much a regulation of rates or a regulation of commerce as is the existing statute. And this consideration is conclusive that there exists no interdependence in the eye of the law between the income-appropriation provisions and the rate-making provisions.

POINT III.

The income-appropriation provisions cannot be sustained as an exercise of the taxing power.

The Circuit Judges in the decision below sustained the provisions in question as an exercise of the power of taxation. After examining the purposes for which the income so appropriated from the carriers was to be used, and concluding that these purposes were purposes for which it would be legitimate for Congress to appropriate public funds, or to raise funds by taxation, the Court said, "While the exaction in question is not denominated a tax, it is in effect an excise tax, levied on

"all carriers subject to the Transportation Act, payable "from surplus earnings", and the Court quoted from the opinion of this Court in the *New England Divisions* case, as follows: "In other words, the additional revenues needed were raised partly by a direct, partly by "an indirect, tax". *Dayton-Goose-creek Railway Co. v. U. S.*, 287 Fed. 728, 732. The language so quoted by the Circuit Judges from the opinion in the *New England Divisions* case was a characterization of the method by which additional revenues were raised, partly by general rate increase, partly by adjustment of divisions. It was not a reference to the income-appropriation provisions of Section 15a, and, if it had been, this Court would not have intended thereby to prejudge any controversy as to the validity of these provisions considered as an exercise of the power of taxation.

This ground of decision was originated by the Circuit Judges themselves. It was not advanced or suggested by Counsel for the Government.

(a) The provisions in question do not purport to be an exercise of the power of taxation.

The Transportation Act 1920, of which these provisions are a part was throughout an exercise of the power to regulate Interstate Commerce. These particular provisions were a part of Title IV, which consisted wholly of amendments to the Interstate Commerce Act, and are a part of Section 15a added as a new Section to the Interstate Commerce Act. We have already pointed out that the primary purpose of new Section

15a was to establish a rule of rate-making which is embodied in paragraphs (2), (3) and (4) of said section. The provisions for the appropriation of a part of the net railway income are introduced by the language in paragraph (5), "Inasmuch as it is impossible (without "regulation and control in the interest of the commerce "of the United States considered as a whole) to establish uniform rates upon competitive traffic", etc. By the language quoted in parentheses Congress expressly labeled the provisions now in question as a regulation and control of commerce. This recital is followed by the declaration that any carrier receiving an income in excess of a fair return shall hold a part of the excess, thereafter prescribed, "as trustee for" the United States. This declaration, made for the purpose of providing a theory by which it was hoped the provisions for appropriating the net railway operation income could be sustained, is the direct opposite of the theory of taxation. It was an attempt to withhold title to the railway earnings from the carriers to the extent that they exceeded a rate prescribed and to divert the title thereto to the United States. Taxation, on the contrary, acknowledges the property to belong to the taxpayer and merely levies a contribution thereon for the purposes of government. Paragraph (6) of the same section provides that one-half of the excess of net railway operating income over 6 per cent. on the property value shall "be recoverable by and paid to the commission". Nowhere in paragraph (5) or paragraph (6) or the subsequent paragraphs dealing with this subject are the

terms "tax", "duty", or "excise" used. It is significant also that the income appropriated is not to be collected by the Treasury Department or administered by that department, but by the Interstate Commerce Commission.

The provisions regarding the one-half of the net railway operating income in excess of six per cent. not required to be paid over to the Commission, further evidence the intent of Congress to act under its commerce power. It is provided that one-half of such excess shall be placed in a reserve fund established and maintained by the carrier, which may be used by the carrier only for the purpose of paying dividends or interest or rent for leased roads to the extent that its net railway operating income for any year is less than six per cent. of its property value, and not for any other purpose. Paragraphs (6), (7) and (8). It is clear that Congress was assuming over the half of the net railway operating income of six per cent. allowed to be retained by the carriers the same dominion and power of control which it exerted as to the half required to be paid to the Commission; this dominion was asserted as to both halves under the power to regulate Interstate Commerce.

Therefore, to hold that the provisions for the appropriation of one-half of the net railway operating income in excess of six per cent. may be sustained as an exercise of the taxing power, is not only to disregard the express declaration of Congress as to the power under which it assumed to be acting, but is to sustain the regulation and control of one-half of the alleged

excess income upon a theory which cannot be advanced for sustaining the regulation and control of the remaining half of the alleged excess income.

A further consideration making against the theory of sustaining these provisions as a tax law is the existence at that time of a very burdensome excess profits tax law. There was then in effect the 1918 Revenue Act, approved February 24, 1919, which besides imposing upon all corporations an income tax of 10 per cent. for 1920 and subsequent years, imposed upon all corporations for those years an excess profits tax of 20 per cent. of net income in excess of the excess profits credit and not in excess of 20 per cent. of invested capital and 40 per cent. of the remaining net income, the excess profits credit being 8 per cent. of invested capital plus \$3,000. These taxes are deducted under the Commission's practice in determining railway operating income. If the part of net railway operating income appropriated by paragraph (6) were considered as a tax, it also would be deductible in ascertaining railway operating income, unless the Commission's practice is changed to differentiate this exaction from other taxes, or unless the complication were avoided by reading into the Act some qualification of the term "net railway operating income".

Again, the 1919 Revenue Act in providing for the ascertainment of taxable net income, for income and excess profits tax purposes, allowed the deduction from gross of all taxes paid under the authority of the United States except income, war-profits and excess-profits

taxes (Sec. 234(a) (3) of 1919 Revenue Act), and if the appropriation of income in paragraph (6) of Section 15(a) of the Commerce Act were sustained as an excise-tax, as held by the Circuit Judges, the amount paid by a carrier therefor would be deductible in its income and excess profits tax returns. This would present another embarrassing circle and complication, requiring for its solution a major operation in statutory construction.

(b) But even if the appropriation of income were labeled as a tax law it would be void because its real purpose, ascertainable from the Act itself, is the limitation of the amount of income which a carrier shall be entitled to retain, an object not within the power of Congress.

We submit that the proposition above stated, falls exactly within the principle of *Bailey v. Drexel Furniture Co.* (Child Labor Tax case), 259 U. S. 20, and *Hill v. Wallace* (The Future Trading Act Case), 259 U. S. 44.

In the *Child Labor Tax* case, there was involved a section of the Revenue Act of 1919 which purported to levy an excise tax of ten per cent. of the net profits of mines, quarries, mills and similar establishments, in which children under the age of fourteen years had been permitted to work. The act was carefully and definitely given the form of a tax law. It was, however, held invalid as being clearly, on its face, designed to penalize and thereby suppress the employment of child labor, the regulation of which is reserved by the con-

stitution exclusively to the States. This Court stated the question presented to be (p. 36): "Does this law impose a tax with only that incidental restraint and regulation which a tax must inevitably involve? Or does it regulate by the use of the so-called tax as a penalty?" Considering only the provisions of the Act itself, the Court concluded (p. 37): "In the light of these features of the act, a Court must be blind not to see that the so-called tax is imposed to stop the employment of children within the age limits prescribed. Its prohibitory and regulatory effect and purpose are palpable." The Court said further at page 37, "It is the high duty and function of this Court in cases regularly brought to its bar to decline to recognize or enforce seeming laws of Congress, dealing with subjects not entrusted to Congress but left or committed by the supreme law of the land to the control of the states." And at page 38, "Taxes are occasionally imposed in the discretion of the legislature on proper subjects with the primary motive of obtaining revenue from them and with the incidental motive of discouraging them by making their continuance onerous. They do not lose their character as taxes because of the incidental motive. But there comes a time in the extension of the penalizing features of the so-called tax when it loses its character as such and becomes a mere penalty with the characteristics of regulation and punishment. Such is the case in the law before us."

In the *Future Trading Act* case there was involved a tax, imposed by that name, of twenty cents a bushel

on contracts for the sale of grain for future delivery, unless the seller owned the grain at the time of sale, or owned or rented the land on which it was to be grown, or unless the contract were made by or through a member of a Board of Trade designated by the Secretary of Agriculture as a contract market, and the Secretary of Agriculture was authorized to designate contract markets only under various prescribed conditions calculated to prevent trading for the purpose of manipulation of prices or the cornering of grain. This Act was held invalid as being completely governed in principle by the Child Labor Tax decision. This Court said (259 U. S. at 66): "It is impossible to escape the conviction, from a full reading of this law, that it was enacted for the purpose of regulating the conduct of business of boards of trade through supervision of the Secretary of Agriculture and the use of an administrative tribunal consisting of that Secretary, the Secretary of Commerce, and the Attorney-General." And again, at page 66: "The Act is in essence and on its face a complete regulation of boards of trade, with a penalty of twenty cents a bushel on all 'futures' to coerce boards of trade and their members into compliance. When this purpose is declared in the title to the bill, and is so clear from the effect of the provisions of the bill itself, it leaves no ground upon which the provisions we have been considering can be sustained as a valid exercise of the taxing power."

While the two decisions above cited advert to the fact that the subject matter Congress there sought to

regulate, under the guise of its taxing power, was a subject matter reserved for the control of the states, this does not affect the application of those decisions to the present case. We have attempted to demonstrate under the preceding points of this brief that the object sought by Congress by the provisions embodied in paragraphs (5) and (6) of Section 15(a) was to regulate the incomes of carriers, and limit the amount of net income which a carrier shall be entitled to retain, not by the regulation of rates, but by a direct appropriation of a part of such incomes arbitrarily determined by Congress to be excessive and that the incomes so appropriated were not the product of rates determined to be unreasonable, but were in all respects the absolute property of the carriers. If we have succeeded in establishing the proposition that the real and primary object of Congress was to regulate incomes by a direct appropriation and seizure of a part of such incomes after they had become the property of the carriers, we have established an object which is within the power, *neither* of Congress *nor* of the state legislatures. No power to limit incomes exists in the states, except to the extent that it may be exercised in the initial grant of franchises and charters. The fact that a field of regulation within the power of the state legislatures was attempted to be invaded by the Child Labor Tax and the Future Trading Tax was not the controlling consideration in these cases. It was enough that the subject matter sought to be regulated was beyond any power of Congress. Where the subject matter, as in this case,

the limitation of incomes by arbitrary and direct appropriation, is withdrawn equally from the power of Congress and from the power of the States, exactly the same principle applies. This Court quoted in its opinion in the *Child Labor Tax* case at page 40 from the opinion of Chief Justice Marshall in *M'Culloch v. Maryland*, 4 Wheat. 316, 423, as follows: "Should Congress, in the execution of its powers, adopt measures which are prohibited by the Constitution; or should Congress, under the pretext of executing its powers, pass laws for the accomplishment of objects not entrusted to the government; it would become the painful duty of this tribunal, should a case requiring such a decision come before it, to say, that such an act was not the law of the land."

We need not distinguish such earlier cases as *Veazie Bank v. Fenno*, 8 Wallace, 533; *McCray v. U. S.*, 195 U. S. 27, and *U. S. v. Doremus*, 249 U. S. 86, in which tax laws have been sustained against an attack alleging that they were enacted with another motive than taxation. These cases are explained and distinguished in the opinion in the *Child Labor Tax* case upon grounds which adequately distinguish them from the present case.

The parallel of the present case, considering the provisions for the appropriation of income as bearing a tax label, with the *Child Labor Tax* and *Future Trading Tax* cases is exact in principle. The facts, so far as they differ, lend added strength to the argument for the invalidity of the alleged or assumed tax in the present case, since in this case the provisions in issue are not

found in a revenue law and do not purport to be adopted under the taxing power. We are, however, disregarding this difference in facts for the purpose of the argument. The Court is not called upon in this case to speculate as to the ulterior motive of Congress or to search outside the terms of the Act itself for such motive. It appears on the face of the Act itself that its purpose was not to raise revenue, with only an incidental effect of limiting incomes, but that its purpose was the regulation of incomes deemed to be excessive in order to avoid public criticism of the rule of rate-making prescribed by Congress. This, as stated, is a subject matter not entrusted to Congress. If then the provisions in question purported to be an exercise of the taxing power, they would fall under the principle of this Court's condemnation of the Child Labor Tax as a pretended exercise of the taxing power which had passed beyond the bounds of that power and asquired predominant characteristics of regulation and punishment.

It follows, therefore, that even if the provisions for the appropriation of income had been characterized by Congress as an imposition of a tax, they could not have been sustained as an exercise of the taxing power.

(c) This appropriation cannot be sustained as a contribution imposed, incidentally to the commerce power, to create the fund called the general railroad contingent fund, as a burden which the industry should bear.

We recognize that Congress, without acting under its taxing power in the strict sense, may under its power

to regulate commerce exact reasonable contributions from carriers for purposes legitimately within the commerce power. We refer to the principle announced in the *Head Money Cases*, 112 U. S. 580, involving an Act of Congress providing for the collection from vessels of fifty cents for each passenger, not a citizen of the United States, transported to the United States from foreign ports, the proceeds to be used as a fund for the care of immigrants and for defraying the expense of administering the Immigration Act. The Court said, page 595, that the power exercised in that Act was not the taxing power, but an incident of the regulation of commerce, and, at page 596: "We are clearly of opinion that, in the exercise of its power to regulate immigration, and in the very act of exercising that power, it was competent for Congress to impose this contribution on the ship owner engaged in that business."

It has not, at this writing, been asserted that the creation of the general railroad contingent fund, for loans to carriers and for the acquisition of railroad equipment and facilities to be leased to carriers, could be deemed the real object of the provisions of paragraphs (5) and (6) of Section 15(a) and that the appropriation of the carrier's income could be sustained as a contribution levied to create that fund as a burden properly to be borne by the industry. But the point may be advanced as a possible phase of the argument under the theory of the taxing power. We believe that such a contention would be far-fetched and without merit.

The creation of the general railroad contingent fund—the name assigned in paragraph (6) to the fund resulting from the seizure of the alleged excess income—was not the *object* of the action of Congress, but merely the disposition or appropriation of the income seized, in other words, a by-product. We refer to the discussion and analysis under the preceding Point I of the real object of Congress, leading to the irresistible conclusion that the primary object was to regulate carrier incomes which Congress considered excessive. The recital in paragraph (5) states in unequivocal terms that the purpose is to take from carriers net railway operating income received by them “substantially and un-reasonable in excess of a fair return”. The Senate Committee report, quoted under Point I, explained that: “It is obvious”, that, in view of the supposed greater assurance of a fair return, “there should be a maximum beyond which an individual carrier shall not be permitted to retain for its own use all it may receive under a given body of rates”. The alleged excess income is declared by paragraph (5) to be held by the carrier “as trustee” for the United States, and by paragraph (6) the method of computing the alleged excess is defined and it is required to be paid to the Commission—all these provisions preceding any reference to the general railroad contingent fund or to the purposes to which the alleged excess to be collected from the carriers shall be devoted. The Court would not be justified in ignoring the facts, and reasoning upon the premises that the creation of a fund, for loaning to carriers and for acquiring

equipment and facilities to be leased to carriers, was the object of the enactment of these income provisions. To warrant such a premise, paragraph (5), which states the purpose and theory of these provisions, should have read to the effect that "Inasmuch as it is desirable and "in the public interest that carriers be aided in financing "expenditures for capital account and refunding maturing securities, and in acquiring railroad equipment "and facilities, and inasmuch as the creation of a fund "for these purposes is a burden which could be borne "by those carriers realizing from their railway operations a net income in excess of a fair return, it is "hereby declared", etc. The foregoing recital, appropriate to the theory now under discussion, is totally different from the form of recital which Congress actually employed as a statement and explanation of the theory of its action.

We call attention in this connection also, as in connection with the consideration of these provisions on the theory of a tax in the strict sense, to the utter inconsistency of the declaration in paragraph (5) that the alleged excess shall be held in trust for the United States. If this were a levy of a contribution to support an object constituting a proper burden of the industry, it would have been neither necessary nor appropriate to declare that the portion of the income exacted for such contribution never belonged to the carrier but was received by it in trust for the United States.

The purposes of the railroad contingent fund, as named in the statute, are undoubtedly purposes for which Congress may appropriate public money under its power to regulate interstate commerce. The designation of these purposes, however, has no more tendency to support the validity of the taking of carrier income than if it had been directed that the amounts collected from the carriers should be covered into the Federal Treasury and be subject to appropriation for all public purposes. If the limited purposes of the fund were controlling in determining the validity of the provisions for taking the income of the carriers, it would be necessary that the purposes, as originally prescribed, should stand intact forever, or at least that any amendments should leave them their character as objects within the commerce power. Of course, this result was never intended; it was designed that the fund collected from the carriers should be under the absolute disposition of Congress at all times.

But, it might be granted, for the purposes of the argument, that the creation of the fund for the purposes described in paragraph (10) was the *object* of the income-appropriation provisions of the statute instead of an incident or by-product of the legislation. These provisions could not be sustained, even on that assumption, for the following reasons:

The burdens in connection with any industry, which may be imposed upon the industry, as an incident of regulation, have a limit. Although that limit has not been defined by this Court and we have no de-

cision as a precedent for the present case, judged in its hypothetical aspect now under examination, even superficial consideration is convincing that the limit of permissible regulation would be exceeded in placing this burden on the industry. The financing of capital expenditures, the refunding of outstanding capital obligations and the acquisition of equipment and other railroad facilities are in their very nature not matters to be provided for through income. The most prosperous carriers could not meet their capital requirements from income, certainly not without depriving their stockholders of all dividends. These purposes call for new capital contributions, normally obtained through securing investors in additional issues of stock and bonds of the carriers. If Congress believes that the Government should assist in providing the new capital constantly required for the proper development of the railroad facilities of the country as a whole, it should do so by appropriations of public funds raised by general taxation. Such a course would make the general public contribute needed additional capital, for the benefit of the whole country, as taxpayers rather than as investors. To consider that these new capital requirements, or any part of them, are a proper burden to be borne by the industry as a whole, through contributions levied upon income or otherwise measured, would exceed any application of this principle of regulation which has ever been advanced.

Noble State Bank v. Haskell, 219 U. S. 104, may be invoked by the Government as a precedent. That

case involved the Oklahoma Bank Depositors Guaranty Fund (which has within recent history demonstrated its economic unsoundness), created by assessment upon all state banks of 1 per cent. (later increased to 5 per cent.) of average deposits, to be used to make good deficiencies due depositors of insolvent banks. This Court held that the State could prohibit the whole business of banking except upon such conditions as it might prescribe and that if the State legislature declared that free banking was a public danger and required this method of financial co-operation as a necessary safeguard, this Court could not interfere. This Court referred to that case in *Mountain Timber Co. v. Washington*, 243 U. S. 219, 245, as involving "a special imposition in the nature of an occupation tax upon all banks existing under the laws of the State". We believe that the *Oklahoma* case does not illustrate the principle which we are now discussing, but that the imposition there involved could not have been sustained except in the case of a business conducted only by the sufferance of the State, and that the power of Congress to regulate interstate commerce is not comparable with the State's power over banking institutions chartered by it. There were decided at the same time with the *Oklahoma* case, and in the same way, *Shallenberger v. First State Bank*, 219 U. S. 114, and *Assaria State Bank v. Dolley*, 219 U. S. 121, involving similar bank guaranty acts of Nebraska and Kansas.

Mountain Timber Co. v. Washington, 243 U. S. 219, in which the Workmen's Compensation Act of the State

of Washington was sustained, is, we believe, the most extreme application of the theory of imposing upon the industry a burden connected with the industry or its regulation which has been adjudicated under any power of regulation not carrying the power of prohibition. This Act classified businesses according to the hazard of injury to employees, imposed upon each employer in those employments classed as hazardous a contribution measured by a percentage of his payroll, which varied from $1\frac{1}{2}$ to 10 per cent. according to the degree of hazard, and devoted the fund so produced to the payment of disability benefits to injured workmen or death benefits to their dependents. This system of compensation excluded private rights of action for injuries, etc. The rates of contribution were declared to be subject to adjustment in the future to carry out the intent that the fund should be merely self-supporting. The act went further than the compensation laws of other states in that it enforced the contributions from an employer, for the benefit of his group, whether or not injuries befell his own employees. This Court stated at page 237 the crucial question to be whether regarding that legislation as a mere exercise of the power of regulation or as a combination of regulation and taxation, it was "not a fair and reasonable exertion of governmental power, but so extravagant or arbitrary as to constitute an abuse of power". For some of the considerations in support of the validity of the law the Court referred to its opinion in *New York Central Railroad v. White*, 243 U. S. 188, concerning the New York Com-

pensation Act, and the opinions in the two cases must be read together. It was considered in the *New York* case, page 201, that the act resulted in a redistribution of the liability or burden resultant from industrial accidents, as it existed under the common law, both the employee and the employer being deprived of certain rights incident to the old system but on the other hand receiving certain advantages. The Court said, page 202, that it could not "ignore the question whether the "new arrangement is arbitrary and unreasonable, from "the standpoint of natural justice". But it considered that the situation dealt with was an employer and employee engaged by mutual consent in a common operation of advantage to both, with more or less probability that the employee would lose his life or suffer injury, with a loss of earning power representing the employee's capital in trade, that such a loss arising out of the business is an expense of the operation as directly as the cost of repairing broken machinery, that on grounds of natural justice it is not unreasonable for the State, while relieving the employer from the greater responsibility for damages under the common law measure, to require him to contribute according to a reasonable and definite scale by way of compensation for the loss of earning power incurred in the common enterprise, through injuries resulting from the employment in which the parties were engaged as co-adventurers. In the *Washington* case, at page 243, the Court said: "We are clearly "of the opinion that a State, in the exercise of its power "to pass such legislation as reasonably is deemed to be

"necessary to promote the health, safety and general
 "welfare of its people, may regulate the carrying on of
 "industrial occupations that frequently and inevitably
 "produce personal injuries and disability with conse-
 "quent loss of earning power among the men and
 "women employed, and, occasionally, loss of life of those
 "who have wives and children or other relations de-
 "pendent upon them for support, and may require that
 "these human losses shall be charged against the indus-
 "try, either directly, as is done in the case of the act
 "sustained in *New York Central R. R. Co. v. White*,
 "*supra*, or by publicly administering the compensation
 "and distributing the cost among the industries affected
 "by means of a reasonable system of occupation taxes."

The *Washington Workmen's Compensation Case*, although the law involved was so extreme as to be sustained by only a bare majority of the Court, falls far short of constituting a precedent for the assessment of the industry to create the general railroad contingent fund. There is not the slightest resemblance between workmen's compensation and the purposes of the general railroad contingent fund. In the compensation cases the industry is required to bear as a cost of operation a measure of the burden of personal injuries inevitably resulting from the conduct of the business. Like other operating costs the amount can be passed on to ultimate consumers. The burden is apportioned among the various enterprises constituting the industry in a proportion determined by the reason for the assessment. It was considered in the compensation

cases that the employer received some consideration for his contributions in the limitation of his common law liability, and also that the assurance of compensation for injuries would to some extent be reflected in wages. The contributions to the general railroad contingent fund, on the contrary, are not a readjustment of any previous liability, cannot be reflected in any degree by reductions of other liabilities or expenses, are assessed upon carriers selected according to their alleged excess net income, a method of selection bearing no relation to the purpose of the contingent fund, and cannot be passed on to the ultimate consumer. This inability to shift the burden is a most important consideration. It may with entire propriety be said that the "industry bears" the cost or the burden in cases where the amounts assessed for any purpose may be treated as operating costs and included in the cost of the product of the business. It is then the whole portion of the public which uses the product of that particular business that bears the cost or burden, as should properly be the case. But when the cost or burden is imposed on the owner of the business in such a manner that it cannot be passed on, it is not "the industry" which bears the cost or the burden, but the owner of the business in his capacity as an investor. The railway operating income appropriated by this law is taken from the stockholders and it continues permanently as their loss or burden.

The purposes of the general railroad contingent fund are not such that the fund can fairly and reasonably be required to be furnished by the carriers' stock-

holders. The purposes are solely capital purposes, namely, the acquisition of additional equipment and facilities or the refunding of old capital obligations. They are essentially different in principle from the making good (so far as money can) the personal injuries suffered by employees in the business, involved in the compensation cases, or the losses of depositors, involved in the bank deposit guaranty cases. The purposes are the physical enlargement or expansion of the various enterprises of the industry, so far as additional facilities and equipment are concerned, and the securing of new investors in such enterprises in place of old investors, so far as refunding is concerned. It may be argued that the stockholders of a public utility undertake to enlarge and add to their facilities as necessary to meet the growing needs of the public. If this be admitted, the obligation is no more than an undertaking to effect the additions to property through new capital supplied by new investors. And, to a great extent, the enlargement of the railroad facilities required to meet the needs of the public involves the building of new lines, an extension of the original undertaking of the stockholders which even the argument of implied obligation cannot be stretched to cover. These capital purposes all call for additional partners or investors in the enterprise. The obligations of the stockholders as to enlargements and additions are, in any event, confined to their own enterprise. To require that the stockholders, through enforced contributions from their income, should provide this new capital for other enterprises

in the industry, would not be consistent with "natural justice", with which this Court in *New York Central Railroad Co. v. White*, *supra*, considered legislation enacted under the theory of burdens of the industry should square.

In this connection and in conclusion, it may be appropriate to correct any assumption that the general railroad contingent fund was a measure of relief particularly designed for the benefit of the "weak roads". Had this been the design of the fund the following language of this Court in *Adkins v. Children's Hospital*, 261 U. S. 525, 557, would be appropriate: "To the extent that the sum fixed exceeds the fair value of the services rendered, it amounts to a compulsory exaction from the employer for the support of a partially indigent person, for whose condition there rests upon him no peculiar responsibility, and therefore, in effect, arbitrarily shifts to his shoulders a burden which, if it belongs to anybody, belongs to society as a whole." The "weak roads" constituted an important phase of the problem confronting Congress in the enactment of the Transportation Act. But the relief, if any, afforded them by the provisions enacted was in the increased revenue which it was hoped the new rule of rate-making would produce. The general railroad contingent fund will aid the "weak roads" less than it will aid the average or the strong roads.

The problem of the "weak roads" was not solved by this enactment. The rule of rate-making on the group basis may be calculated to effect some improvement in the earnings of the weak roads, but it is inherent in this rule that the weak roads will earn less than the average roads of the group and, therefore, will realize less than a "fair return". The general railroad contingent fund established through the appropriations of income made from the stronger roads is to be used either by making loans to carriers to meet expenditures for capital account or to refund maturing securities or for acquiring transportation equipment and facilities to be leased to carriers. Such loans are required to be made at 6 per cent, and are restricted to cases in which the prospective earning power of the carrier and the security offered by it furnish reasonable assurance of its ability to repay the loan. Leases of equipment and facilities acquired with this fund may be made only when the Commission finds that the prospective earning power of the carrier furnishes reasonable assurance of its ability to pay the rental and meet its other obligations under the lease, and the rental charges must be such as to pay a return of 6 per cent. and an allowance for depreciation upon the valuation of the equipment or facilities so leased. [Paragraphs (10) to (14) of Section 15a.] It would appear doubtful whether, under these restrictions, the general railroad contingent fund will be at all available to the weak roads for aid in new financing or refunding of old obligations or in acquiring equipment and additional facilities,—certainly the fund is not designed for their special and particular benefit.

From a consideration of the committee reports and an analysis of the pertinent provisions of the law as enacted, the conclusion is irresistible that the income appropriation provisions have little, if any, relation to the problem of the weak roads, but are designed simply to prevent the realization by the stronger roads of a net railway operating income in excess of an amount which Congress was willing they should retain.

October, 1923.

Respectfully submitted,

JOSEPH PAXTON BLAIR
 EDGAR H. BOLES
 JOHN F. BOWIE
 ROBERT J. CARY
 HENRY W. CLARK
 HERBERT FITZPATRICK
 LAWRENCE GREER
 W. S. HORTON
 WILLIAM S. JENNEY
 E. W. KNIGHT
 RICHARD V. LINDABURY
 WILL H. LYFORD
 SAMUEL W. MOORE
 WILLIAM CHURCH OSBORN
 WINSLOW S. PIERCE
 HENRY V. POOR
 JOHN H. AGATE
 CARL A. DE GERSDORFF

As Amici Curiae.



APPENDIX.

Text of Section 15a of the Interstate Commerce Act, as added by Section 422 of the Transportation Act, 1920.

41 Statutes-at-Large 488.

“(1) When used in this section the term “rates” means rates, fares, and charges, and all classifications, regulations, and practices, relating thereto; the term “carrier” means a carrier by railroad or partly by railroad and partly by water, within the continental United States, subject to this Act, excluding (a) sleeping-car companies and express companies, (b) street or suburban electric railways unless operated as a part of a general steam railroad system of transportation, (c) interurban electric railways unless operated as a part of a general steam railroad system of transportation or engaged in the general transportation of freight, and (d) any belt-line railroad, terminal switching railroad, or other terminal facility, owned exclusively and maintained, operated, and controlled by any State or political subdivision thereof; and the term “net railway operating income” means railway operating income, including in the computation thereof debits and credits arising from equipment rents and joint facility rents.

“(2) In the exercise of its power to prescribe just and reasonable rates the Commission shall initiate, modify, establish or adjust such rates so that carriers as a whole (or as a whole in each of such rate groups or territories as the Commission may from time to time designate) will, under honest, efficient and economical management and reasonable expenditures for maintenance of way,

structures and equipment, earn an aggregate annual net railway operating income equal, as nearly as may be, to a fair return upon the aggregate value of the railway property of such carriers held for and used in the service of transportation: *Provided*, That the Commission shall have reasonable latitude to modify or adjust any particular rate which it may find to be unjust or unreasonable, and to prescribe different rates for different sections of the country.

“(3) The Commission shall from time to time determine and make public what percentage of such aggregate property value constitutes a fair return thereon, and such percentage shall be uniform for all rate groups or territories which may be designated by the Commission. In making such determination it shall give due consideration, among other things, to the transportation needs of the country and the necessity (under honest, efficient and economical management of existing transportation facilities) of enlarging such facilities in order to provide the people of the United States with adequate transportation: *Provided*, That during the two years beginning March 1, 1920, the Commission shall take as such fair return a sum equal to $5\frac{1}{2}$ per centum of such aggregate value, but may, in its discretion, add thereto a sum not exceeding one-half of one per centum of such aggregate value to make provision in whole or in part for improvements, betterments or equipment, which, according to the accounting system prescribed by the Commission, are chargeable to capital account.

“(4) For the purposes of this section, such aggregate value of the property of the carriers shall be determined by the Commission from time to time and as

often as may be necessary. The Commission may utilize the results of its investigation under section 19a of this Act, in so far as deemed by it available, and shall give due consideration to all the elements of value recognized by the law of the land for rate-making purposes, and shall give to the property investment account of the carriers only that consideration which under such law it is entitled to in establishing values for rate-making purposes. Whenever pursuant to section 19a of this Act the value of the railway property of any carrier held for and used in the service of transportation has been finally ascertained, the value so ascertained shall be deemed by the Commission to be the value thereof for the purpose of determining such aggregate value.

"5. Inasmuch as it impossible (without regulation and control in the interest of the commerce of the United States considered as a whole) to establish uniform rates upon competitive traffic which will adequately sustain all the carriers which are engaged in such traffic and which are indispensable to the communities to which they render the service of transportation, without enabling some of such carriers to receive a net railway operating income substantially and unreasonably in excess of a fair return upon the value of their railway property held for and used in the service of transportation, it is hereby declared that any carrier which receives such an income so in excess of a fair return, shall hold such part of the excess, as hereinafter prescribed, as trustee for, and shall pay it to, the United States.

"(6) If, under the provisions of this section, any carrier receives for any year a net railway operating

income in excess of 6 per centum of the value of the railway property held for and used by it in the service of transportation, one-half of such excess shall be placed in a reserve fund established and maintained by such carrier, and the remaining one-half thereof shall, within the first four months following the close of the period for which such computation is made, be recoverable by and paid to the Commission for the purpose of establishing and maintaining a general railroad contingent fund as hereinafter described. For the purposes of this paragraph the value of the railway property and the net railway operating income of a group of carriers, which the Commission finds are under common control and management and are operated as a single system, shall be computed for the system as a whole irrespective of the separate ownership and accounting returns of the various parts of such system. In the case of any carrier which has accepted the provisions of section 209 of this amendatory Act the provisions of this paragraph shall not be applicable to the income for any period prior to September 1, 1920. The value of such railway property shall be determined by the Commission in the manner provided in paragraph (4).

“(7) For the purpose of paying dividends or interest on its stocks, bonds, or other securities, or rent for leased roads, a carrier may draw from the reserve fund established and maintained by it under the provisions of this section to the extent that its net railway operating income for any year is less than a sum equal to 6 per centum of the value of the railway property held for and used by it in the service of transportation, determined as provided in paragraph (6); but such fund shall not be drawn upon for any other purpose.

"(8) Such reserve fund need not be accumulated and maintained by any carrier beyond a sum equal to 5 per centum of the value of its railway property determined as herein provided, and when such fund is so accumulated and maintained the portion of its excess income which the carrier is permitted to retain under paragraph (6) may be used by it for any lawful purpose.

"(9) The Commission shall prescribe rules and regulations for the determination and recovery of the excess income payable to it under this section, and may require such security and prescribe such reasonable terms and conditions in connection therewith as it may find necessary. The Commission shall make proper adjustments to provide for the computation of excess income for a portion of a year, and for a year in which a change in the percentage constituting a fair return or in the value of a carrier's railway property becomes effective.

"(10) The general railroad contingent fund so to be recoverable by and paid to the Commission and all accretions thereof shall be a revolving fund and shall be administered by the Commission. It shall be used by the Commission in furtherance of the public interest in railway transportation either by making loans to carriers to meet expenditures for capital account or to refund maturing securities originally issued for capital account, or by purchasing transportation equipment and facilities and leasing the same to carriers, as hereinafter provided. Any moneys in the fund not so employed shall be invested in obligations of the United States or deposited in authorized depositories of the United States subject to the rules promulgated from

time to time by the Secretary of the Treasury relating to Government deposits.

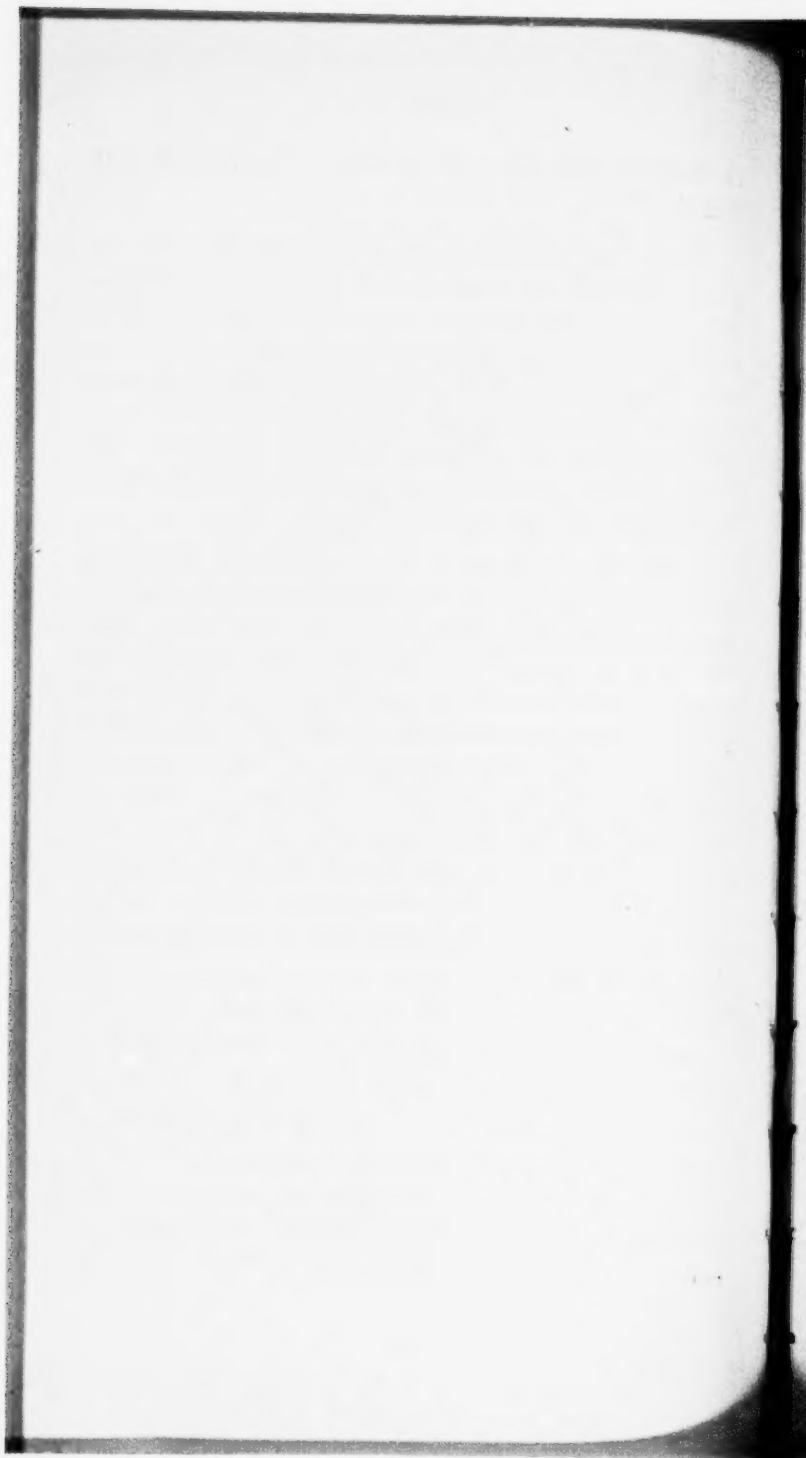
“(11) A carrier may at any time make application to the Commission for a loan from the general railroad contingent fund, setting forth the amount of the loan and the term for which it is desired, the purpose of the loan and the uses to which it will be applied, the present and prospective ability of the applicant to repay the loan and meet the requirements of its obligations in that regard, the character and value of the security offered, and the extent to which the public convenience and necessity will be served. The application shall be accompanied by statements showing such facts and details as the Commission may require with respect to the physical situation, ownership, capitalization, indebtedness, contract obligations, operations, and earning power of the applicant, together with such other facts relating to the propriety and expediency of granting the loan applied for and the ability of the applicant to make good the obligation, as the Commission may deem pertinent to the inquiry.

“(12) If the Commission, after such hearing and investigation, with or without notice, as it may direct, finds that the making, in whole or in part, of the proposed loan from the general railroad contingent fund is necessary to enable the applicant properly to meet the transportation needs of the public, and that the prospective earning power of the applicant and the character and value of the security offered are such as to furnish reasonable assurance of the applicant's ability to repay the loan within the time fixed therefor, and to meet its other obligations in connection with such loan, the Commission may make a loan to the applicant from

such railroad contingent fund, in such amount, for such length of time, and under such terms and conditions as it may deem proper. The Commission shall also prescribe the security to be furnished, which shall be adequate to secure the loan. All such loans shall bear interest at the rate of 6 per centum per annum, payable semiannually to the Commission. Such loans when repaid, and all interest paid thereon, shall be placed in the general railroad contingent fund.

“(13) A carrier may at any time make application to the Commission for the lease to it of transportation equipment or facilities, purchased from the general railroad contingent fund, setting forth the kind and amount of such equipment or facilities and the term for which it is desired to be leased, the uses to which it is proposed to put such equipment or facilities, the present and prospective ability of the applicant to pay the rental charges thereon and to meet the requirements of its obligations under the lease, and the extent to which the public convenience and necessity will be served. The application shall be accompanied by statements showing such facts and details as the Commission may require with respect to the physical situation, ownership, capitalization, indebtedness, contract obligations, operation, and earning power of the applicant, together with such other facts relating to the propriety and expediency of leasing such equipment or facilities to the applicant as the Commission may deem pertinent to the inquiry.

“(14) If the Commission, after such hearing and investigation, with or without notice, as it may direct, finds that the leasing to the applicant of such equipment or facilities, in whole or in part, is necessary to enable the applicant properly to meet the transporta-



OCT 22 1923

WM. R. STANSBURY

CLERK

Supreme Court of the United States,

OCTOBER TERM, 1923.

No. 330.

DAYTON-GOOSE CREEK RAILWAY COMPANY,

Appellant,

vs.

THE UNITED STATES OF AMERICA, THE INTER-
STATE COMMERCE COMMISSION, AND RAN-
DOLPH BRYANT, UNITED STATES DISTRICT
ATTORNEY FOR THE EASTERN DISTRICT OF
TEXAS.

Appeal from the District Court of the United States for the
Eastern District of Texas.

BRIEF

Asserting that it is the true economic value of railroad property, determined as in
a condemnation case, to which the recapture provisions of Paragraph (6) of
Section 15a, Interstate Commerce Act, are applicable.

SAMUEL W. MOORE,

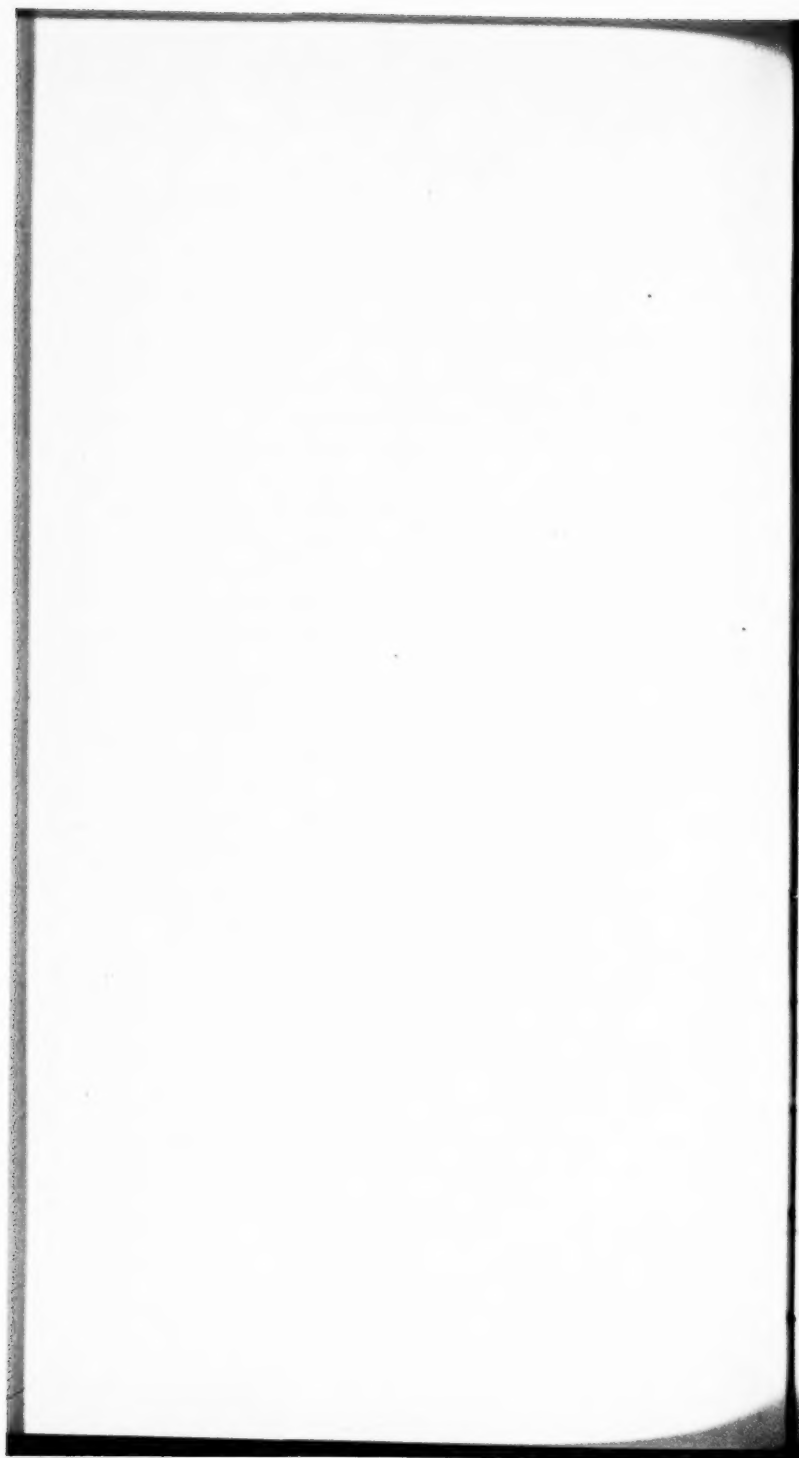
as Amicus Curiae.

October 20, 1923.



INDEX.

	PAGE
Statement	1
Point I. It is contended that the Valuation Act, for the purpose of the recapture clause, requires the ascertainment of economic value, and that the economic value of railroad property bears a relation to the income which it affords. If this be true, it cannot be said, in advance of the ascertainment of such economic value, that the Dayton-Goose Creek Railway Company has any excess earnings subject to recapture.....	3
1. The economic value of railroad property bears a relation to the income which it affords	10
2. The valuation of competing railroads cannot be controlled by the principles applicable to the valuation of monopolistic utilities..	16
3. There is no "vicious circle" involved in giving weight to earning power in the determination of the economic value of railroad property	18
4. Assuming that the Act requires the ascertainment of economic value, how is it to be determined?	25
5. The Fifth Amendment prohibits the use of any "sum" or cost figure less than the true or economic value of the property....	30



Supreme Court of the United States,

OCTOBER TERM, 1923.

No. 330.

DAYTON-GOOSE CREEK RAILWAY
COMPANY,
Appellant,

vs.

THE UNITED STATES OF AMERICA, THE
INTERSTATE COMMERCE COMMISSION,
and RANDOLPH BRYANT, UNITED
STATES DISTRICT ATTORNEY FOR THE
EASTERN DISTRICT OF TEXAS.

APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES
FOR THE EASTERN DISTRICT OF TEXAS.

Statement.

By leave of Court, the undersigned submits this brief as *amicus curiae* in the interest and behalf of The Kansas City Southern Railway Company upon the question of "the value of railroad property" which is to be taken

as a basis or starting point in the computation of excess earnings under Section 15a of the Interstate Commerce Act.

The Interstate Commerce Commission, which is charged with the enforcement of the recapture provisions of the Act, has apparently decided that the value of railroad property is not an economic, but an equitable concept; that the value upon which the exempt six per cent. is to be computed is a "sum" determined largely upon original cost, or cost of reproduction less depreciation, and called "a value for rate-making purposes", but bearing no relation to the exchange value or economic value of the property. Apparently, this so-called "value for rate-making purposes" is to be used by the Commission in the computation of the earnings of all railway companies or systems which have net railway operating income in any year in excess of six per cent. on such value.

It is believed that the so-called "value for rate-making purposes" is not *value* in any true sense, and that it is not *the value* required by the Valuation Act. It is asserted, on the contrary, that the value of railroad property on which the exempt six per cent. is to be computed is its true or economic value, as such value would be determined in a condemnation proceeding.

Inasmuch as one of the questions raised in this case is the "kind" of value of railroad property to which the recapture provisions are to be applied, it has been thought proper to file this brief in the hope that it may be helpful to the court in its consideration of this ques-

tion. It is intended hereby to supplement the arguments contained in other briefs asserting the unconstitutionality of the recapture provisions.

POINT I.

It is contended that the Valuation Act, for the purpose of the recapture clause, requires the ascertainment of economic value, and that the economic value of railroad property bears a relation to the income which it affords. If this be true, it can not be said, in advance of the ascertainment of such economic value, that the Dayton-Goose Creek Railway Company has any excess earnings subject to recapture.

On March 1, 1913, the Valuation Act, now Section 19a of the Interstate Commerce Act, was approved, requiring the Interstate Commerce Commission to investigate, ascertain and report "the value" of all the property owned or used by every common carrier subject to the provisions of the Act. By the Transportation Act, 1920, the values so fixed by the Commission are required to be used for the recapture of excess earnings, for the purpose of consolidation, for the issuance of securities, and other governmental purposes.

Nearly, if not quite ten years ago contentions began before the Commission over the "kind" of value it was required to ascertain under the act, that is, whether it should be economic value, or something different, and

these contentions are still going on. So far, the Commission, in two final value cases—San Pedro, Los Angeles & Salt Lake Railroad Company and Atlanta, Birmingham & Atlantic Railroad Company—handed down September 11, 1923, has found what it denominates “a value for rate-making purposes” which does not purport to be true or economic value. Thus, it has found a value of \$23,245,257 for the Atlanta, Birmingham & Atlantic Railroad—a road which, up to valuation date, had not earned its operating expenses, and of which the Commission said (75 I. C. C. 668):

It does not now appear what changes, if any, the future will bring, but measured by all standards the expenditure of money on the road as of date of valuation were not justified by the service then rendered or the prospects of service within a reasonable period of time.

Mr. Commissioner Potter, in a dissenting opinion, described the hopelessness of this enterprise in even more forceful language, saying (p. 672):

Probably no one would assert that the property of the A., B. & A. is worth anything like \$10,000,000. Certainly no sane person would pay that amount for it. All of its securities could be bought for a smaller sum. It never has been and never can be worth that much. Neither past, present, nor prospective earnings indicate the possibility of any such value. It can not succeed as a legitimate business enterprise. It is not needed. It ought never to have been built, and, considered as a separate line, at least, it should be abandoned. Its assured and deserved destiny is to be scrapped,

unless it is absorbed in consolidation. In view of these facts, which I think we all know, I see no justification for according to this property a value of nearly \$24,000,000.

If this so-called value of "nearly \$24,000,000" stands, it must be added to the group value, and rates must be made which will yield $5\frac{3}{4}$ per cent thereon. Thus shippers will be required to pay a return on a value which Mr. Commissioner Potter regards as largely fictitious.

In the *San Pedro, Los Angeles & Salt Lake R. R.* case, apparently the same methods of valuation were applied, resulting in a so-called "value for rate-making purposes" in the sum of \$45,000,000. The evidence adduced in the case, indicating a valuation of approximately \$75,000,000 on the basis of earning power, was not accepted by the Commission.

The Commission evidently has made no effort thus far to ascertain economic value, but has contented itself with the determination of "a value for rate-making purposes." This it ascertains by the use of what amounts to a formula applied to cost figures, with the addition of land values determined by the average value of adjoining non-carrier lands. No actual consideration, and certainly no weight, has been given to the respective earning capacities of these two properties. There is no pretense that the Commission's figures represent, or were intended to represent, pecuniary or economic value.

It appears from an address by Mr. Leslie Craven at the annual meeting of the American Bar Association, August 28, 1923, entitled "Railroad Valuation: A State-

ment of the Problem," that at that time the Commission had issued 329 tentative valuations, the aggregate value found for the properties reported on being \$2,898,000,000. He says, in explanation of the methods employed:

An analysis of the figures shows that a cost formula has been generally employed although the same formula has not been applied in every case. In a very large number of cases, and in so great a number that obviously it is not by mere coincidence, it occurs that the addition of the cost of reproduction less depreciation, and the acreage value for non-railway purposes of the land, together with a sum which is 5% of the preceding two amounts, will produce a figure, to which the "final value" (reported in *round* figures) is very close. Taking the 329 tentative valuations as a whole, the final value found is 5.6% in excess of the aggregate cost of reproduction less depreciation and land value figures. Speaking generally, a cost method has been used for all railroads with no regard for their relative productivity, or the existence or non-existence of the qualities which determine value in any true sense.

The foregoing is referred to merely for the purpose of illustrating one concept of value, which we insist is not value at all, but which the Commission apparently has accepted, and which it calls "value for rate-making purposes." This school of thought treats value, not as an economic thing, but as an equitable concept, variously expressed by "what is fair" or "what is just and reasonable" or "what is right."

Judge Prouty, as Director of Valuation, in his memorandum in the Texas Midland case, pages 2 and 3, described his conception of value for rate-making purposes as that "sum, upon which, under all the circumstances and upon a fair consideration of all the facts and elements to be taken into account, a fair return should be permitted." This is evidently the conception of value adopted by the Commission.

We contend that such value, when used as the basis of an action for the recapture of excess earnings, is unreal and fantastic, and not the value protected by the Fifth Amendment; and this contention will be considered later.

The other concept of value, which we believe to be the true one and which has been urged upon the Commission in the course of its proceedings under the Valuation Act, is economic value, exchange value or pecuniary value, all of which mean one and the same thing. This school of thought treats value as "power in exchange," as the market value, as the amount which a willing purchaser but not compelled to purchase, would be willing to pay, and a willing seller but not compelled to sell, would be willing to accept. It is the value which would measure "just compensation" in a condemnation suit.

It is true that while the securities of a railroad company may have a market value, yet railroad properties themselves are not customarily bought and sold in the market so as to establish a market value. But the Valuation Act obviously intended that the Commission should ascertain the true economic or exchange value of railroad

properties, as an equivalent or substitute for their market value.

Value is thus defined by this court in *International Harvester Co. v. Kentucky*, 234 U. S. 216, 222:

Value is the effect in exchange of the relative social desire for compared objects expressed in terms of a common denominator.

This is a definition of exchange value. It is the value which would be awarded the owner of railroad property if it were taken by the Government in the exercise of its power of eminent domain. It is the value on which a railway company is constitutionally entitled to earn a fair return. It is the value on which properties are consolidated, on which securities are issued, and taxes paid. It is very far removed from an arbitrary "sum"—determined without any standard, and without chart, compass or guide—upon which "a fair return should be permitted." The Fifth Amendment protects private property to its full value; if it merely protected an arbitrary "sum," it would be so vague and indefinite as to be unenforceable.

The Valuation Act was passed after value had been defined by this court as above quoted, and Congress is presumed to have known of this judicial definition and to have used the word in its economic sense (*Thorn v. Browne*, 257 Federal 523). Certainly, Congress had in mind the Fifth Amendment, for it was careful to preserve to each carrier six per cent. upon the value of its railroad property. It is clear that if Congress had defined excess income as net railway operating revenue over

and above six per cent. upon an arbitrary "sum" bearing no relation to economic value, determined by no rules or standard, but resting in the inner consciousness of the individual who fixed it, such six per cent., so computed, could not for a moment be regarded as a compliance with the amendment. Undoubtedly, Congress intended that the six per cent. should be applied to the true or economic value of railroad property, determined in accordance with established principles. Otherwise the six per cent. provision would be meaningless. It is not conceivable that there can be different values for different purposes, any more than that there can be different units of weight and measure for different purposes. When "the value" required to be ascertained by the statute has been found, it is the value for all purposes (*Havre de Grace Bridge Co. v. Towers*, 132 Md. 16, 103 Atl. 319; *State ex rel. Oregon R. & Nav. Co. v. Clausen*, 63 Wash. 535, 116 Pac. 7; *State ex rel. Bee Bldg. Co. v. Savage*, 65 Neb. 714, 91 N. W. 716; *Re Raritan River Co.*, P. U. R. 1915-E, 72).

If railroad property is taken in the exercise of the power of eminent domain, the compensation to which the owner is entitled is "the full and perfect equivalent of the property taken," and this includes interest on its value until the compensation is paid (*Seaboard Air Line* case, decided March 3, 1923). The taking of the title to private property for public use, and the taking of the use of private property in the public interest, are one and the same thing in principle, and both are equally protected by the limitations of the Fifth Amendment. This is the holding of the *Reagan* case (154 U. S. 362, 410), where,

in an action to enjoin a schedule of rates alleged to be confiscatory, the court said:

If the state were to seek to acquire the title to these roads, under its power of eminent domain, is there any doubt that constitutional provisions would require the payment to the corporation of just compensation, that compensation being the value of the property as it stood *in the markets of the world*, and not as prescribed by an act of the legislature? Is it any less a departure from the obligations of justice to seek to take not the title but the use for the public benefit at less than its *market value*?

It is to be noted that the use of railroad property for the public benefit may not be taken at less than its "market value," and that the value of the property "as it stood in the markets of the world" is the value protected by the constitutional provision. There is no intimation that some arbitrary "sum" deemed fair and just shall be the criterion.

The constitutional guaranty extends to the use of property as well as to the property itself (*Buchanan v. Warley*, 245 U. S. 60; *Brooks-Scanlon Co. v. R. R. Comm.*, 251 U. S. 396; *Northern Pacific R. Co. v. North Dakota*, 236 U. S. 585; *Norfolk & Western R. Co. v. Conley*, 236 U. S. 605).

1. *The economic value of railroad property bears a relation to the income which it affords.* It is entirely plain, we respectfully submit, that it is the true or economic value of railroad property to which the provisions of the recapture clause must be applied. How is that

value to be ascertained and determined? It appears to be fairly well settled that the economic value of property bears a relation to the income which it affords; that value results from the use to which the property is put, and varies with the profitableness of that use, present and prospective, actual and anticipated, and that the amount and profitable character of such use determines the value. A brief reference will now be made to some of the cases in this court where this rule has received approval.

This court in *South Utah Mines & Smelters v. Beaver County*, a tax case decided May 21, 1923, held that the value of property does bear a relation to its income, saying:

The value of property bears a relation to the income which it affords. If it be property whose production is uniform and of indefinite duration the capitalization of the net income derived from it at the going rate of interest, in the absence of a more certain method, will furnish a reasonable measure of the value.

In *Branson v. Bush*, 251 U. S. 182, 187, the same principle is stated, where the value of railroad property was under consideration, the court saying, quoting from *R. R. Co. v. Backus*, 154 U. S. 439:

But the value of property results from the use to which it is put, and varies with the profitableness of that use, present and prospective, actual and anticipated. There is no pecuniary value outside of that which results from such use. The amount and profitable character of such use determines the value.

In *Monongahela Nav. Co. v. U. S.*, 148 U. S. 312, a lock and dam in the Monongahela River were condemned by the Government, and the question arose as to the compensation to which the owner was entitled. It was held that the owner was entitled to "the full equivalent therefor", and this was measured by the value of the property, and this value was determined, not by the mere cost of construction, but by the earnings of the property, which largely determine its value. The court said (p. 328):

How shall just compensation for this lock and dam be determined? What does the full equivalent therefor demand? The value of property, generally speaking, is determined by its productiveness—the profits which its use brings to the owner. Various elements enter into this matter of value. Among them we may notice these: Natural richness of the soil as between two neighboring tracts—one may be fertile, the other barren; the one so situated as to be susceptible of easy use, the other requiring much labor and large expense to make its fertility available. Neighborhood to the centers of business and population largely affect values. For that property which is near the center of a large city may command high rent, while property of the same character, remote therefrom, is wanted by but few and commands but a small rental. Demand for the use is another factor. The commerce on the Monongahela river, as appears from the testimony offered, is great; the demand for the use of this lock and dam constant. A precisely similar property, in a stream where commerce is light, would naturally

be of less value, for the demand for the use would be less. The value, therefore, is not determined by the mere cost of construction, but more by what the completed structure brings in the way of earnings to its owner. For each separate use of one's property by others, the owner is entitled to a reasonable compensation, and the number and amount of such uses determines the productiveness and the earnings of the property, and, therefore, largely its value.

So, in valuing railroad property, various elements enter into the matter of value; the efficiency of the transportation plant, its capacity to handle an increased volume of traffic without additional capital expenditures, its strategic position, its terminals, its nearness to large centers of population and to centers of industry and commerce, the location and character of its competing lines, the volume of traffic naturally tributary to its rails, the permanency of such traffic and its possible further development and increase, its gradients, curvature, costs of operation, and many other circumstances, all of which contribute, in a greater or lesser degree, in determining its earning power. For each separate use of his property, the owner is entitled to a reasonable compensation, and the number and amount of such uses determines the productiveness and the earnings of the property, and therefore largely its value. In other words, the value of railroad property bears a relation to the income which it affords.

In *Omnia Commercial Co. v. U. S.*, decided by this court on April 9, 1923, reference is made to the *Mononga-*

hela case, supra, and after quoting therefrom, the court said:

The lock and dam constituted, in effect, a going concern, whose value was of course affected by what it would produce.

In *Adams Express Co. v. Ohio State Auditor*, 166 U. S. 185, the property of an express company, both intangible as well as tangible, had been assessed at \$4,189,818. The value of its tangible property was \$1,159,491. The company insisted that it should be assessed only at the lower figure; but this contention was denied by the court, saying:

It is worth \$4,189,818 for the purpose of income to the holders of the stock and for the purposes of sale in the markets of the land. * * * The value which property bears in the market, the amount for which its stock can be bought and sold, is the real value. Business men do not pay cash for property in moonshine or dreamland. They buy and pay for that which is of value in its power to produce income, or for the purpose of sale.

In *St. Louis & East St. Louis Electric R. Co. v. Missouri*, decided May 2, 1921, the question was the value of .346 of a mile of track in the State of Missouri, assessed at \$186,019, of which \$13,019 represented tangible, and the remainder intangible property. It was objected that the assessment should be limited to the value of the tangible property, but it was held that the company possessed certain valuable contracts which gave to its property the higher value, the court saying:

It was these contracts which gave the company's small extent of physical property *an earning capacity, and therefore a value.*

In *Cudahy Packing Co. v. Minnesota*, 246 U. S. 450, it appeared that a gross revenue tax of the State of Minnesota was imposed upon the car line of the Packing Company. It was contended that the tax should be limited to the cash value of the cars, taken separately, but this court held that the State might tax the property "at its real value as a part of a going concern", saying:

The record makes it reasonably certain that the property, *valued with reference to its use and what it earns*, is worth considerably more than the cash value of the cars taken separately.

A similar question was decided in *Union Tank Line v. Wright*, 249 U. S. 275, where the court said:

While the valuation must be just, it need not be limited to the mere worth of the articles considered separately, but may include as well "the intangible value due to what we have called the organic relation of the property in the state to the whole system."

¹ In *Louisville & Nashville R. Co. v. Greene*, 244 U. S. 522, the court said, in speaking of the methods of determining the value of railroad property for taxation:

In such cases there are (at least) two recognized methods, known as the stock-and-bond plan and the capitalization of income plan. In the present case the latter was followed.

2. *The valuation of competing railroads can not be controlled by the principles applicable to the valuation of monopolistic utilities.* It will tend to clearness of thought if we bear in mind the essential distinction between the valuation of public utilities, such as a water company or a gas company, located in a single municipality, and the valuation of competing railroads, operated under the same rates but with different costs of operation and different volumes of traffic. A water company, for example, operates in a single municipality and without competition. Rates or charges are established for it by public authority, and for it alone. If its net revenue is deemed too great by those who make the rates, the rates, and therefore the revenue, may be reduced, in the absence of a binding contract to the contrary. If the net revenue is deemed too small, the rates, and therefore the net revenue, may be increased. The rate-making body deals directly with this one utility and is in a position at all times to control its revenues. In these circumstances, the law has laid down a rule for the ascertainment of the value of the utility, or rather its rate base, on which it is entitled, in any event, to earn its constitutional return, and as much more as the rate-making authority may permit. This rule is to take cost of reproduction new, computed at current prices, deduct depreciation, add the value of land and a more or less arbitrary sum for going concern, and the result is called value, or, more properly, a rate base.

Competing railroads occupy an essentially different position. Published rates, applicable to the service of

transportation which they perform, must of necessity be the same between competing points, as well as upon competing commodities. If this were not so, traffic, which like water seeks the lowest level, would flow over the road with the lowest rates to the exclusion of its competitors and to the confusion and disorganization of railroad operation. The operating cost on each road will be different, due to density of traffic, gradients, and many other causes. The volume of traffic will likewise vary on each road. It is axiomatic that competing carriers under the same rates, with varying costs of operation and varying volumes of traffic, will have widely varying profits, and these profits will bear no direct relation to original cost, or cost of reproduction, or cost of reproduction less depreciation, or other physical circumstances or characteristics. The outstanding feature is that while rates and charges of a public utility are fixed for it alone, and the rate-making power is thus enabled to control its revenue, in the case of railroad companies the rate-making power can not deal directly with each individual carrier and fix rates and charges for it alone, and thus control its revenue; but, on the contrary, the rates and charges of competing railroads are not based upon the value of any individual road, but upon the aggregate value of railway property in each competing group, with the result that the net income of the individual members of a competing group will depend upon what they can earn under rates which are the same for all. It is thus that the "strong" roads with a good earning power, and "weak" roads with a lower earning

power, are developed. It is not practicable for the rate-making authorities to establish still lower rates (even if the law permitted them to do so) for the purpose of reducing the net earnings of the strong lines, for the result of such an effort would be to still further impoverish the weak lines, with resulting bankruptcy and inability to render the service which the public demands. So long as this condition exists, the so-called strong lines will enjoy larger net revenues and possess a correspondingly greater value than the so-called weak lines. That different carriers have different earning power is recognized in paragraph (5) of Section 15a of the Interstate Commerce Act, where it is said:

Inasmuch as it is impossible (without regulation and control in the interest of the commerce of the United States considered as a whole) to establish uniform rates upon competitive traffic which will adequately sustain all the carriers which are engaged in such traffic, etc.

The essential difference between monopolistic public utilities, operating in a single city, whose income can be increased or decreased at the will of the appropriate rate-making power, and competing railroads operating under uniform rates, but with different operating costs and volumes of traffic, and with widely different earning power, should, we respectfully submit, be constantly borne in mind.

3. *There is no "vicious circle" involved in giving weight to earning power in the determination of the eco-*

nomic value of railroad property. Many arguments have been levelled against the use of earning capacity under reasonable rates in the determination of value. It is urged that under this theory, value is made to depend upon rates, and rates in turn are determined by the value thus fixed, and so, it is said, we go around in a circle. Judge Prouty, in his Memorandum upon Final Value, page 7, has stated the argument as follows:

A rate-making value is to be stated for the purpose of determining a fair rate. Commercial value is determined by the rates actually in effect. If, therefore, commercial value is to determine the rate, then the present rates must be right.

Judge Prouty's criticism might be justified in the case of a water works operating in a single municipality, without competition. If its earning capacity under existing rates indicates a net revenue of, say, \$6,000,000 per year, year after year, as far as the future can reasonably be predicted, this would be six per cent. annually upon \$100,000,000, and the latter sum would fairly represent its value on a six per cent. basis. By taking this value as a starting point to determine what rates should be charged, and assuming that the plant is entitled to six per cent., or \$6,000,000 per year, it will, of course, be found that the rates necessary to yield that return are the rates in effect at the time under consideration. The same might be true in the valuation of railway property if there were but one railroad in the country, so that the rate-making power would be enabled to deal with it directly.

But Judge Prouty's criticism fails entirely when applied to existing conditions, where we have a large number of carriers operating in competition with each other. As before stated, the railways of the country operate in competing groups, with the same rates between competitive points but with different operating costs and with different volumes of traffic, and, therefore, widely different earning capacities. It is impossible for the rate-making authority to deal with each carrier individually. If the Commission could do that which is impossible—that is, make separate rates for each carrier between competitive points, and make these rates dependent upon the value of each carrier's property—then Judge Prouty's criticism might be a just one, since, in that case, as in the case of the water works, value would depend upon the rate, and, in turn, the rate could be made to depend upon value.

But rates applying to competing carriers can not be made separately upon the value of each individual line. Prior to the Transportation Act, they were made by the Commission by a consideration of all the lines in a competing group—the strongest as well as the weakest—the aim being to make the rate for the group fit the average condition. After the passage of that Act a rate base was created, consisting of the aggregate value of the railroad properties in each group. The rates must be so constructed as to yield a given percentage on the aggregate value in each group. The group value, therefore, and not the value of the individual road, is the unit that must be dealt with in the making of rates.

The rate base for the Western Group is \$8,100,000,000. Rate schedules which are calculated to yield six per cent. on this sum are conclusively presumed to be reasonable. They are made so by the Transportation Act. The net earnings of individual carriers in the group, under the rates so made, will, of course, differ widely. The earning capacity of each carrier will largely determine its commercial value. But this commercial value of each individual carrier (\$653,033, the Commission's value in the case of the Dayton-Goose Creek) does not determine what the rates shall be. That depends upon the \$8,100,000,000 rate base. If the value of the Dayton-Goose Creek, or of any other individual line, were doubled or trebled, or wiped out altogether, the effect on the rate level in the group would be negligible. There is, therefore, no "circle" involved in taking the aggregate value in the group as a rate base, and basing rates thereon, and using the net earnings of each individual line, under such rates, as a factor in its commercial value.

Again, the courts are unanimous in holding that where a schedule of reasonable rates has been lawfully determined by the legislative authority, the earning power of a given carrier is a proper and important matter for consideration in the determination of its value. The plain reason is that, as in ordinary commercial and industrial enterprises (not subject to public regulation), earning capacity under prices and charges fixed in the open market determines the value, so in the case of enterprises subject to public regulation, the prices and charges fixed by public authority are in lieu of and in substitu-

tion for those which otherwise would be fixed in the public market. If earnings under competition-made prices are an important factor in fixing value, so must be earnings under commission-made prices, since the commission fixes prices which would be fixed by free competition if it existed. This thought is well expressed in *Utilities Commission v. Springfield Gas Co.*, 291 Ill. 209, 219, where it is said:

Fixing rates by public authority may secure to each individual the advantage of collective bargaining by all in behalf of the whole body of consumers and result in such a rate as might properly be supposed to result from free competition, if free competition were possible.

In this connection, it should be borne in mind that the Commission itself, in its thirtieth annual report, dated December 1, 1916, declared, in substance, that all rates then in effect were reasonable and asked Congress to so declare by statutory enactment. It said (p. 78):

All rates, fares and charges have been open to complaint for a period of more than ten years, within which the Commission had power to fix the future maximum rates. For a period of more than six years all proposed increased rates have been subject to protest and suspension before becoming effective. Obviously, there should come a time when as to the past the general level of the rates and the relationship of rates should be fixed as reasonable. We are convinced that the best interests of the entire public, of the system of governmental regulation of rates, and of railroads,

will be served by the enactment of a statute which, as of a specified date, fixed the existing interstate rates, fares, classifications, rules, regulations and charges as just and reasonable for the past, and which provides that after that date no change therein may be made except upon order of the Commission. Of course, causes pending at the time of the enactment of such a statute should be preserved. The time as of which the existing rates, fares, charges, classifications, rules and regulations are declared to be reasonable for the past should antedate somewhat the date of the enactment, in order to prevent the filing of numberless complaints and new rate schedules in anticipation of a date fixed at some time in the future.

Not only does the Commission itself say, in substance, that its rates then in effect were reasonable, but there is a "strong presumption" in favor of the reasonableness of rates made by an experienced administrative body after full hearing (*Darnell v. Edwards*, 244 U. S. 564). The Commission having the power to fix future maximum rates and to suspend all proposed rates before becoming effective, the strongest presumption exists that all uncontroverted rates are at all times reasonable. Furthermore, while a schedule of rates is in force, the legal effect is precisely the same as if an act of Congress had been passed specifically prescribing each individual rate contained in the many schedules (230 U. S. 197; 271 Fed. 449). Surely, no one would seriously question that earnings under rates so established would be competent evidence of economic value.

It is always to be borne in mind that the reasonableness of rates is not to be tested by the amount of revenue which a railway company may receive from its entire rate schedules, nor is it to be tested by the mere value of the property employed in the service of transportation. The reasonableness of the charge for each service which a carrier may perform is the unit to be taken and considered as a separate and distinct problem. If the particular charge for that specific service is reasonable from the standpoint of the shipper as well as from the standpoint of the carrier, the rate is reasonable; otherwise not. For each particular service performed by the carrier it is entitled to a reasonable charge. The number and profitable character of such charges, present and prospective, will determine its earning capacity, and will afford the best measure of its value. In the *Monongahela* case, *supra*, where the charges were subject to public regulation, the rule is stated as follows:

For each separate use of one's property by others, the owner is entitled to a reasonable compensation, and the number and amount of such uses determine the productiveness and earnings of the property, and, therefore, largely, its value.

To the same effect are *Cotting v. Godard*, 183 U. S. 79; *Canada Southern R. Co. v. International Bridge Co.*, L. R., 8 App. Cas. 723, 731; *R. R. Comm'rs v. Illinois Central*, 20 I. C. C. 181.

There is still another reason why earning capacity may legitimately be given consideration. As before

stated, the railroads composing a competing group or competing groups will have varying earning powers. Some may be strong roads, and others weak roads. The strong roads will have a differential in earning power over the weaker lines, and this differential will continue to exist as rates and revenues increase or decrease. While it is true that the Government possesses the power to reduce rates, and so to reduce earnings; and while it is not probable that the Government would ever exercise such a power oppressively or unjustly, yet there is a practical limit to the exercise of the power. The railroads are the arteries of commerce, and must be maintained in as high a state of efficiency as the transportation service which they afford, respectively, requires or demands. It is not conceivable that a policy destructive of existing railroads would be pursued by the Government; on the contrary, the demand of the people that existing systems of transportation be preserved and improved, can not be ignored; and any administration that persisted in thinking otherwise would be short-lived.

4. *Assuming that the Act requires the ascertainment of economic value, how is it to be determined?* If it be true, as appears to be abundantly established by authority, that the value of property does in fact bear a relation to the income which it affords; that such value is increased as the company becomes prosperous and its net railway operating income becomes greater; and that such value is lessened when such income decreases, these principles should be applied to ascertain the true value of

the Dayton-Goose Creek property, and, when such value is ascertained, to apply to it the recapture provision.

Property is valuable in the judgment of mankind for what it will produce; its productivity or earning capacity, past, present and future, is the chief factor from which the judgment of value is derived. But before earning capacity can be determined, the physical property, in all its parts and in all its relations, must be considered and examined with the greatest care; and when earning capacity has once been determined, it is the ultimate factor of greatest importance, for it has merged or swallowed up a consideration of every element of the property, whether tangible or intangible, that tends, directly or remotely, presently or in the future, toward the production of income or the incurring of expense. An intelligent survey of the future prospects of a property is a most important factor, since value is a judgment largely resting upon prophecies of the future, based upon known conditions of the past and present. It is the uncertainties of the prophecies of future operation and future returns that make value so much a matter of varying judgment among men who have equal knowledge or equal opportunities for knowledge. If we could look into the future and see events as they would later transpire; if, for illustration, we could look into the future sufficiently to ascertain and determine with accuracy the net railway operating income of the Dayton-Goose Creek Railway, or of any other carrier, from year to year indefinitely in the future, business men would take these figures, apply the discounts, and

reach a judgment of value, on which they would be willing to buy or sell, with astonishing unanimity. The same would be true of any other industrial or commercial enterprise in the country.

There is a general consensus of opinion that property is worth an amount on which it will produce an assured income at the going rate of interest. This rule does not apply to speculative property, where the risk is considerable and the rate of return is not reasonably steady and assured. When we think of the value of bonds, stocks and farm lands, we think of the amount on which the investment will pay the going rate of interest.

It is the same with railroad property—it has no pecuniary value outside of its ability to produce income. The value of such property is ordinarily thought of in terms of income, and as the amount of money upon which the income will provide the going rate of interest. It was doubtless in recognition of this rational and almost universal conception of value that this court said, in *South Utah Mines & Smelters v. Beaver County*, *supra*:

If it be property whose production is uniform and of indefinite duration the capitalization of the net income derived from it at the going rate of interest, in the absence of a more certain method, will furnish a reasonable measure of the value.

The capitalization of the income of railroad property is the standard and recognized method of valuing it for purposes of taxation (*Louisville & Nashville R. Co. v. Greene*, 244 U. S. 522).

Let us, therefore, apply this method of valuation to the Dayton-Goose Creek property, as we may assume some court or commission would do, in the ascertainment of its true or economic value.

Its net railway operating income for 1921 amounted to \$72,948. The property, therefore, from the standpoint of income, was at that time the equivalent of a well-secured promissory note bearing and paying annual interest in the sum of \$72,948. The value of the note, or its principal sum, in ordinary commercial usage is ascertained by capitalizing the amount of the annual interest at the going rate, which may be assumed to be six per cent. The sum thus computed would be \$1,215,800. If we further assume that \$72,948 had been and would continue to be the annual income of the property, this amount, under the authorities above quoted, would justify a finding by court or commission that that was the value of the Dayton-Goose Creek property on the basis of its earning capacity. If it was earning the same amount prior to the passage of the Transportation Act, and its value fixed by court or commission at that sum as of that date, the prospective passage of that Act, with its recapture provision, would not reduce this value, because there would be no earnings in excess of six per cent. of such value, and hence no threatened loss of revenue by recapture. It was then, and still is, entitled to earn six per cent. on its true value; and it has earned that amount, and no more.

Let us go a step farther and assume that the earnings of the Dayton-Goose Creek property, instead of

continuing substantially the same from year to year, have an annual upward trend; that is, that the earnings of the property, as it is fair to assume is the case with the great majority of the railroads of the country, are increasing to some extent from year to year, and that the indications are that, based upon past experience and trends, its net earnings for 1922 will be greater than in 1921, and for 1923 greater than in 1922, and so on. In this event, a court or commission would be justified in finding that the economic value of the property in 1921 would be a greater sum than the capitalized earnings of that year; and as the immune six per cent. must needs be computed upon such greater value, it is even clearer that there would be no excess earnings subject to recapture. That this is so will appear from the following considerations.

A definition of value approved by experience is as follows:

The value of a thing is measurable by the sum of the amounts expected to be received from it, discounted to the time of expected receipt.

In the case of a progressive increase in net earnings after valuation date, 1921, an intending purchaser would make his computation of the amounts reasonably expected to be received from the operation of the railroad properties over a period of, say, ten years, estimating from the best available sources the probable net income for each year of the period, and would then discount these amounts to the time of expected receipt, and would estimate the value of the property accordingly. If the

increased earnings for a ten-year period succeeding 1921 could be ascertained with anything like accuracy, the value of the property could then be ascertained; the precise method to be employed being to add to the capitalized earnings for the year 1921 the present worth at six per cent. bank discount of the capitalization at six per cent. of the increase for each year. But, of course, future earnings must be estimated, and can not be ascertained with accuracy. But we are not concerned, for the moment, with the accuracy of the estimate. The fact that the earnings are increasing is sufficient in itself to demonstrate that the value of the property in 1921 should be something more than a capitalization of its net railway operating income of that year. By so much, therefore, is the property removed from the operation of the recapture provision.

5. *The Fifth Amendment prohibits the use of any "sum" or cost figure less than the true or economic value of the property.* Let us assume that the Commission decides to value all railroad property at its original cost, upon the theory that whatever was prudently invested in the property in the course of its history, and no more, is the investment which the law protects; in other words, exchange value, which bears a relation to the income which the property produces, is to be discarded, and original cost substituted therefor. What would be the result?

The first result immediately apparent would be that the railroads of the country would be valued upon different bases. Those constructed many years ago, when

prices of land, materials and labor were low, would be upon a lower basis, and those recently constructed under higher corresponding prices, would be upon a much higher basis. The old pioneer roads, which had first come into the field, and which have done the most to promote and develop the commerce of the country, would receive the least favorable treatment; the newest roads, which had recently come into existence, would become the favorites of the law.

But the most serious result of the application of this doctrine would be the utter confiscation of all property values in excess of original cost. For illustration, a railroad was constructed many years ago, when prices of land, materials and labor were comparatively low, and this railroad has brought about, or contributed to bringing about, the development and prosperity of the country which it serves, so that real estate prices have doubled or trebled, terminal properties have increased by leaps and bounds, and there has been an actual increase in the value of its land and physical property to the extent of \$1,000,000. But the road is to be limited to six per cent. upon its original cost, and by the time original cost is to be taken as value, the recapture provision may have sufficiently advanced and developed so that *all* in excess of six per cent. is taken by the Government; and nothing remains, therefore, to the carrier except six per cent. upon its "prudent" investment.

The effect, of course, would be to reduce the value of the property to the amount of its cost; no sane man would pay more than that for it, for the reason that it could not, under any circumstances, earn more than six

per cent. thereon. The \$1,000,000 enhanced value, or "unearned increment", as it is sometimes called, is wiped out. It is a typical case of confiscation. Can this be done consistently with the provisions of the Fifth Amendment?

The officials of the railroad might well point out that other owners of private property were permitted to share in the general prosperity of the country, and that the law protected them in the enjoyment of their property to its full economic value, even though such value had increased as the result of such general prosperity, and they might protest against the palpable injustice of applying one rule to the valuation of railroad property and another and more favorable rule to all other property. The stockholders might well point out that their investment in the railroad property, though deemed "prudent" in the eye of the law, was most unfortunate in fact, since it might have been made in other property which enjoyed the privilege of keeping pace with the general increase in values throughout the country.

The increase in value of railroad property over its original cost is not limited to increase in land values, as in the foregoing illustration, but extends to all other factors and elements which enter into and determine economic value. For illustration, a railroad was constructed many years ago, when prices were low, through a comparatively undeveloped part of the country, at a cost of \$50,000,000. Since its original construction, large and important cities have grown up along its line and at its terminals, a great number of important industries have been located on or adjacent to its line, its grades

have been reduced to three-tenths of one per cent., its cost of operation is extremely low in comparison with other companies, its traffic has increased many fold and is still increasing. This property, by reason of its location, its low grades, its very large volume of traffic, is able to earn handsome returns under rates under which its competitors can barely keep out of a bankruptcy court. Even if rates continue to be made so low as to barely enable its competitors to exist, this road will have current net earnings, and an assurance of a continuation and increase thereof in the future, sufficient to justify a economic value of \$500,000,000. It could be sold any day for that amount. If the Government should condemn it, it would be compelled to pay that amount, or more. It earned in the year 1922 a net railway operating income of \$30,000,000, which is six per cent. of its economic value, as above set forth, or sixty per cent. upon its original cost. Is it obliged to pay to the Government one-half of the excess of six per cent. upon its original cost, which would be \$13,500,000? Or may it say to the Government that the true or economic value of its property is \$500,000,000; it has earned six per cent. thereon; there are no excess earnings, and it owes the Government nothing? May it further say to the Government that the value of its private property—that is, the “full and true equivalent” of its private property—is \$500,000,000, and that, under these circumstances, to limit its value to its original cost of \$50,000,000 is nothing short of confiscation, prohibited by the organic law?

Under the Fifth Amendment, private property, measured by a value which is the full and perfect equivalent

therefor, may not be taken for public use without just compensation. The amendment is a limitation upon the power of the general government, and what the general government would have to pay in the event that it condemns a railroad property for public use is the measure of protection which the amendment affords when it undertakes to take the use of the property in the public interest, as it does when it fixes rates to be charged which are required to provide just compensation for such use. There can be no controversy over the character of the value of railroad property which the Government would be required to pay if it undertook to condemn it. It would be the true economic value, or exchange value, or pecuniary value, all of which mean market value, where that is available, or the equivalent of market value, where that is not available.

If the railroad property in either of the above illustrations were being condemned by the Government, and counsel for the Government should say that its value in such a proceeding is measured by the original cost, rather than by its higher market value or economic value, no one will contend that such a position would command serious consideration. Every one will concede that the true economic value, regardless of cost, is the only criterion in a condemnation case. This is so because the Fifth Amendment protects the owner of private property to the extent of its full and perfect pecuniary equivalent, which is its true economic value. But the same amendment affords the same protection to a railway company where the use of its property in the public interest is

being taken. In the one case, the title is taken for public use; and in the other, the use is taken in the public interest. The value which the amendment protects is precisely the same, and that value is determined by the rules applicable in condemnation proceedings.

Had the intention of the people in adopting the amendment been otherwise, different phraseology would have been employed. The "property" of which one shall not be deprived without due process of law, and the "private property" which may not be taken for public use without just compensation, would have been qualified by some such clause as "provided that Congress may fix the value of such property at such sum as it sees fit." This, of course, would have destroyed the protection afforded by the amendment. Congress could then constitutionally fix value at some insignificant sum.

The advocates of the cost theory of valuation might as well say that one-half of cost, or any other fraction thereof, should be taken as the value protected by the Fifth Amendment. If any sum less than true economic value of property can be taken as its value, then there is no limit beyond which the whittling down process may not go.

What is said above of original cost applies equally to cost of reproduction; cost of reproduction less depreciation, or any other cost figures, or any other arbitrary concepts of value less than the true economic value.

Respectfully submitted,

SAMUEL W. MOORE,
as Amicus Curiae.

25 Broad Street,
New York, N. Y.

October 20, 1923.

FILED

NOV 12 1923

WM. R. STANSBURY

CLERK

Supreme Court of the United States,

OCTOBER TERM, 1923.

No. 330.

DAYTON-GOOSE CREEK RAILWAY COMPANY,
Appellant,

vs.

THE UNITED STATES OF AMERICA, THE INTER-
STATE COMMERCE COMMISSION, AND RANDOLPH
BRYANT, United States District Attorney for the Eastern
District of Texas.

APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES
FOR THE EASTERN DISTRICT OF TEXAS.

BRIEF

Directed to the proposition that the income-appropriation provisions of Section 15a of the Interstate Commerce Act are unconstitutional on the face of the statute because they fix as a just return a rate of return which is so low as to be confiscatory, and which, by reasons of its uniformity and consequent inflexibility, is so unreasonable as to constitute a taking of property without due process of law.

WINSLOW S. PIERCE,
LAWRENCE GREER,
F. C. NICODEMUS, JR.,
As Amici Curiae.

October 29, 1923.

PRINTED IN THE U. S. BY C. G. BURGOYNE PRINTING BUSINESS, 107 LIBERTY STREET, NEW YORK



Supreme Court of the United States,

OCTOBER TERM, 1923.

No. 330.

DAYTON-GOOSE CREEK RAILWAY
COMPANY,
Appellant,

vs.

THE UNITED STATES OF AMERICA,
THE INTERSTATE COMMERCE
COMMISSION, and RANDOLPH
BRYANT, UNITED STATES DIS-
TRICT ATTORNEY FOR THE EAST-
ERN DISTRICT OF TEXAS.

**APPEAL FROM THE DISTRICT COURT OF THE
UNITED STATES FOR THE EASTERN
DISTRICT OF TEXAS.**

Statement.

By leave of Court, the undersigned, attorneys and counsellors of this Court, submit this brief as *amici curiae* in the interest and behalf of Wabash Railway Company, Western Maryland Railway Company and St. Louis Southwestern Railway Company, directed to the single question whether the rate of return fixed by the income-appropri-

tion provisions of Section 15a of the Interstate Commerce Act is a fair and just rate of return for all carriers subject to the Act.

The General Counsel of the Kansas City Southern Railway Company has filed a brief directed to the question of "the value of railroad property", to which the income-appropriation provisions of Section 15a are applicable.

Not conceding but ignoring for purposes of this argument, all questions as to the method to be adopted or the formula to be applied in ascertaining that "value" which is referred to in the income-appropriation provisions of Section 15a, and assuming that such "value" is properly ascertained and determined, it is our purpose to supplement the Kansas City Southern Company's argument, as well as the arguments contained in other briefs, asserting the unconstitutionality of these provisions, by a brief argument directed to the one controlling proposition that the statute is unconstitutional on its face because these provisions fix as a just return on such "value" a rate of return which is so low as to be confiscatory, and which by reason of its uniformity and consequent inflexibility is so unreasonable as to constitute a taking of property without due process of law.

ARGUMENT.

Insofar as Section 15a of the Interstate Commerce Act attempts to deprive a carrier of one-half of its net railway operating income in excess of six per cent. of the aggregate value of the railway property held for and used by the carrier in the service of transportation without regard to (a) the character and condition of the carrier; (b) the location of its railway property, and (c) the money rates and economic conditions prevailing where its railway property is situated, the statute is unconstitutional on its face.

Excepting only the argument originated by the Circuit Judges that the income-appropriation provisions of Section 15a are valid as an exercise of the taxing power, all of the arguments advanced in support of this statute are mere restatements of the proposition that Congress in the exercise of its power to regulate Commerce may lawfully confiscate a part of an interstate rail carrier's railway operating income, provided only that the part which remains unappropriated constitutes a fair return upon the aggregate value of the railway property held for and used by the carrier in the service of transportation.

An analysis of Section 15a will show conclusively that Congress legislated upon the assumption that a return of six per cent. upon the aggregate value of the carrier's railway property constitutes a fair return, and that any income in excess of six per cent. lies outside of the protection of the Fifth Amendment.

It is our contention that six per cent. is not a fair return upon railway property in any part of

the country, but if we are wrong as to this and it is believed that six per cent. is a fair return upon railway property in some parts of the country, then we submit that Section 15a is unconstitutional and void because it attempts to fix six per cent as a proper rate of return on railway property in every part of the country.

The subject of the rate of return protected by Fifth Amendment was considered by this Court in the recent case of *Bluefield Water Works & Improvement Company v. Public Service Commission of the State of West Virginia, et al.*, decided June 11, 1923, and this Court then held that six per cent. was not a fair return upon the value of property of a corporation serving water to the city of Bluefield, West Virginia, and its inhabitants.

Inasmuch as the part of the opinion in this case written by Mr. Justice Butler, relating to the rate of return, reviews all of the previous authorities and furnishes a complete text for the argument against the rate of return attempted to be fixed by Section 15a, we quote in full this part of the opinion:

“The state commission found that the company's net annual income should be approximately \$37,000, in order to enable it to earn 8 per cent for return and depreciation upon the value of its property as fixed by it. Deducting 2 per cent for depreciation, there remains 6 per cent on \$460,000, amounting to \$27,600 for return. This was approved by the state court.

“The company contends that the rate of return is too low and confiscatory. What annual rate will constitute just compensation depends upon many circumstances and must be determined by the exercise of a fair and

enlightened judgment, having regard to all relevant facts. A public utility is entitled to such rates as will permit it to earn a return on the value of the property which it employs for the convenience of the public equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties; but it has no constitutional right to profits such as are realized or anticipated in highly profitable enterprises or speculative ventures. The return should be reasonably sufficient to assure confidence in the financial soundness of the utility, and should be adequate, under efficient and economical management, to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties. A rate of return may be reasonable at one time, and become too high or too low by changes affecting opportunities for investment, the money market, and business conditions generally.

"In 1909, this court in *Willcox v. Consolidated Gas Co.*, 212 U. S. 19, 48-50, 53 L. ed. 382, 393, 399, 48 L. R. A. (N. S.) 1134, 29 Sup. Ct. Rep. 192, 15 Ann. Cas. 1034, held that the question whether a rate yields such a return as not to be confiscatory depends upon circumstances, locality, and risk, and that no proper rate can be established for all cases; and that, under the circumstances of that case, 6 per cent was a fair return on the value of the property employed in supplying gas to the city of New York, and that a rate yielding that return was not confiscatory. In that case the investment was held to be safe, returns certain, and risk reduced almost to a minimum,—as nearly a safe and secure investment as could be imagined in regard to any private manufacturing enterprise.

"In 1912, in *Cedar Rapids Gaslight Co. v. Cedar Rapids*, 223 U. S. 655, 670, 56 L. ed. 594, 604, 32 Sup. Ct. Rep. 389, this court declined to reverse the state court where the value of the plant considerably exceeded its cost, and the estimated return was over 6 per cent.

"In 1915, in *Des Moines Gas Co. v. Des Moines*, 238 U. S. 153, 172, 59 L. ed. 1244, 1253, P. U. R. 1915D, 577, 35 Sup. Ct. Rep. 811, this court declined to reverse the United States district court in refusing an injunction upon the conclusion reached that a return of 6 per cent per annum upon the value would not be confiscatory.

"In 1919, this court in *Lincoln Gas & E. L. Co. v. Lincoln*, 250 U. S. 256, 268, 63 L. ed. 968, 976, 39 Sup. Ct. Rep. 454, declined, on the facts of that case, to approve a finding that no rate yielding as much as 6 per cent on the invested capital could be regarded as confiscatory. Speaking for the court, Mr. Justice Pitney said:

'It is a matter of common knowledge that, owing principally to the World War, the costs of labor and supplies of every kind have greatly advanced since the ordinance was adopted, and largely since this cause was last heard in the court below. And it is equally well known that annual returns upon capital and enterprise the world over have materially increased, so that what would have been a proper rate of return for capital invested in gas plants and similar public utilities a few years ago furnishes no safe criterion for the present or for the future.'

"In 1921, in *Brush Electric Co. v. Galveston*, the United States district court held 8 per cent a fair rate of return.

"In January, 1923, in *Minneapolis v. Rand*, the circuit court of appeals of the eighth circuit (258 Fed. 818, 830) sustained, as against

the attack of the city on the ground that it was excessive, $7\frac{1}{2}$ per cent, found by a special master and approved by the district court as a fair and reasonable return on the capital investment—the value of the property.

“Investors take into account the result of past operations, especially in recent years, when determining the terms upon which they will invest in such an undertaking. Low, uncertain, or irregular income makes for low prices for the securities of the utility and higher rates of interest to be demanded by investors. The fact that the company may not insist as a matter of constitutional right that past losses be made up by rates to be applied in the present and future tends to weaken credit, and the fact that the utility is protected against being compelled to serve for confiscatory rates tends to support it. In this case the record shows that the rate of return has been low through a long period up to the time of the inquiry by the commission here involved. For example, the average rate of return on the total cost of the property from 1895 to 1915, inclusive, was less than 5 per cent; from 1911 to 1915, inclusive, about 4.4 per cent, without allowance for depreciation. In 1919, the net operating income was approximately \$24,700, leaving \$15,500, approximately, or 3.4 per cent on \$460,000 fixed by the commission, after deducting 2 per cent for depreciation. In 1920, the net operating income was approximately \$25,465, leaving \$16,265, for return, after allowing for depreciation. Under the facts and circumstances indicated by the record, we think that a rate of return of 6 per cent upon the value of the property is substantially too low to constitute just compensation for the use of the property employed to render the service.”

From the foregoing it is obvious that the six per cent. rate—the lowest this Court has ever approved—if not already obsolete by reason of changed conditions, cannot properly be accepted as a fair and constitutionally valid return upon the property of a rail carrier.

Every condition or consideration which this Court mentions as a justification for the six per cent. rate in the few cases in which it has been approved, is absent in the case of a rail carrier. The element of monopoly which is stressed by Mr. Justice Butler is wholly absent. The reverse of that condition is conspicuously present. The rail carrier enjoys no monopoly but, on the contrary, it conducts a business and devotes its property to a business which is highly competitive and which the Transportation Act, 1920, expressly provides shall continue to be competitive. The element of stability in earning power which is also stressed by Mr. Justice Butler is again absent. The rail carrier does not have an income so stable as to be "virtually guaranteed" (we quote Justice Pitney) but, on the contrary, its income is subject to violent fluctuations in response to the changing tides of commerce. Although in times of business depression our great urban populations must continue to consume gas, light and power at usual and customary rates, railway revenues may be held at a level so low that even the so-called "strong roads" cannot earn the expenses of operation.

Disregarding the uncertain, if not mercurial character of railway revenues and railway operating income, Section 15a attempts to put the rail carrier in the same category as a monopoly with an income "virtually guaranteed" and as-

serts congressional power to confiscate in any year the income in excess of six per cent. although for a long period of previous years the carrier's income may have fallen below six per cent. Obviously, this statute, if it becomes effective, will operate to prevent a carrier from setting up proper reserves out of the earnings of prosperous years to cover periods of depression, so that sooner or later the accumulated surpluses of even the so-called "stronger roads" will yield to the attrition of lean years and our rail transportation systems will be legislated into receivership and bankruptcy.

Plainly, a rate of return which is fair and just for a monopolistic, non-competitive enterprise with an earning power "virtually guaranteed" and so situated that "the risk is reduced almost to a minimum" is confiscatory when applied to a rail carrier subject to the countless vicissitudes of interstate commerce.

In the New York Consolidated Gas Company case Mr. Justice Peckham, in that part of his opinion quoted by Mr. Justice Butler, says that no proper rate of return can be established for all cases. Yet that is precisely what Congress attempts to do under the income-appropriation provisions of Section 15a—it attempts to fix for all cases and for all carriers the six per cent. rate as the level above which legislative confiscation of railway income is beyond the protection of the Fifth Amendment. Thus it arbitrarily fixes a rate applicable to all carriers throughout the country, which rate, by reason of its uniformity and consequent inflexibility, must necessarily disregard the character and condition of the individual carrier, the location of its railway property and

the money rates and economic conditions prevailing where its railway property is situated, all of these being vital factors which this Court says cannot be disregarded.

For the foregoing reasons we contend that the income-appropriation provisions of Section 15a should be declared unconstitutional on the face of the Act.

Respectfully submitted,

WINSLOW S. PIERCE,
LAWRENCE GREER,
F. C. NICODEMUS, JR.,
as Amici Curiae.

37 Wall Street,
New York, N. Y.

October 29, 1923.